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BUSINESS ORGANISATION

(For B. Com. Classes)

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PREFACE TO THIRD EDITION

It is very gratifying to note that a new edition of this book has been called for within two years of the publication of the last edition. Opportunity has, therefore, been taken to revise the entire text, and to exclude those portions which were considered rather ambitious for B. Com. students.

Test questions taken from the University examination papers have been added after each chapter.

It is confidently hoped that this new edition will admirably meet the requirements of those for whom it is principally meant.

Nawalgarh :
30th April 1945. }

R. R. G.

PREFACE TO FIRST EDITION

This book has been written principally for the use of students preparing for the B. Com. Examination of Indian Universities. Business Organisation is an important subject included in the B. Com. syllabus, but the various existing books on the subject are either too ambitious or too sketchy. Unless a student reads a number of them, he cannot be expected to have faithfully covered the whole course proscribed. This Book is intended to remove this difficulty.

The author does not claim any originality for the subject-matter of this book. The material has been very carefully collected from numerous sources, and is presented in a form in which it may be easily grasped by young students.

The author hereby acknowledges with gratitude the assistance he has received from the various standard books on the subject.

30th June 1945.

R. R. G.

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business. We can realise this to best purpose by considering the word 'organ'. If we talk of the human body as an organism, we shall find that the separate parts are often called organs. The heart and the lungs and the liver are organs. This will illustrate for us the fact that organisation is not a mere gathering together of a number of working parts to perform a certain final operation. The heart must beat, the lungs must breathe, the liver must perform its purifying operations in order that the man may live. Each function is absolutely necessary to the fullness of the man's life. Each organ is organised to fulfil its own particular mission so that the complete organism may fulfil its own completed mission.*

Having grasped the meaning of the term organisation, let us try to examine the factors that make for success in business. As a rule, every business requires certain resources in the form of capital, equipment, workers, etc.; and, above all, it needs a capable organiser for its successful running. The man who runs the show is the first requisite for every successful business. What qualities then should a good business organiser possess? This is not an easy question capable of an easy and definite answer. If we were to ask a number of successful business men on what factors the success of each of them depended, it is almost certain that we would not get the same reply from each. People start business in different circumstances, and in each case success is won by different qualities possessed by the proprietors. As a result of this inquiry, we shall, however, learn that business success is not achieved as cheaply as many persons imagine. In fact, there is no royal road to success in any walk of life, much less in business.

It is not, therefore, possible to lay down any hard and fast rules for the guidance of business men so that they may always win success. But at the same time there are a number of qualities that must ordinarily be possessed by one who wants to succeed in business. These qualities were ably analysed by an eminent business man, Sir Edward Benthall of Messrs. Bird & Co., Calcutta, in the course of a lecture which he delivered in 1939 under the auspices of the Appointments and Information Board of the Calcutta University. This is what he said.

Now I will try to analyse for you the question: What are the qualifications for success?

Many years ago, when I first entered into business, I jotted down some maxims uttered by a very well-known business leader on a similar occasion. These have often and often come back to my mind since, and I cannot do better today than to repeat them with the addition of certain comments of my own.

* F. F. Sbarles, *Business Building* Vol. II,

1. *Eliminate the word 'perfunctory' in any task.* Your work in any task will testify in some way for or against you. On this axiom I would comment that undoubtedly the successful execution of any plan or policy in any walk of life depends largely on minute attention to detail. And that is no less true of business than of other careers. Hard work continuously is the only way to business success and mere presence on the job is not sufficient, for it is not the hours you put in that count, but what you put into the hours. If you put all that is best in you into your work, however unimportant it may seem, you are bound to be noticed by your superiors and you will have taken the first step to promotion. Opportunities will follow either for advancement in the business to which you are apprenticed or to start your own concern. One reason why so few people recognise opportunity is because it is disguised as hard work. Sooner or later a chance will come and then you must seize it with both hands.

2. *The most serviceable of all assets is reputation. It works twenty four hours a day for you.* The most valuable asset you can possess in business is credit, which means the confidence of other people in your character. If people trust you, even though your resources are not great, they will give you credit. If, for instance, a Bank trusts your individual character, they will advance you money against far less security than if they have any doubts about your integrity. If indeed there is doubt about the latter, you may not get credit on any conditions whatsoever. Credit is earned by a lifelong adherence to the truth. One slip and your credit may be ruined for ever, just as once a man has taken a bribe his credit is for ever gone.

Remember, too, that if you are to become associated with the management of public companies, you will be in a fiduciary position and will have to carry the confidence of the shareholders. Your greatest asset will be their trust. Things may go wrong, but whether it is through your own mismanagement or through sheer bad luck, they will trust you if you are straightforward with them and their confidence will stand you in good stead.

3. *Think. Exercise your brain as you do your muscles.* The most valuable thing which the education that you have received up to date can have taught you is how to think. It is probable that very little of what you have actually learnt in the way of facts during your academic career, will be of any value to you whatsoever in a business career, but if you have learnt how to think for yourself and how to apply the knowledge that you will constantly be picking up throughout life, you will go on learning things of value. In business one never ceases to learn, and you can learn from studying the means and methods of other communities such as the Marwaris or Europeans. We have no more than you in the way of mental equipment, and often very much less. But in business the possession of a degree in itself is of no value whatsoever. The value lies in

the extent to which your mind has been trained in the course of your academic career to correlate values and to form a sound judgment.

4. *Go for a ride on the horse of your imagination occasionally.* It is a good thing to dream dreams, but as the poet said, it is better to do lovely things, not dream them. You cannot build a reputation on what you are going to do. Dream dreams occasionally by all means, but rely on your own activity to make them come true. Let one of your dreams be to be master of your own business or head of the company you serve, but live to make it come true.

5. *Be ready, but know how to wait. Presevere in the face of hope deferred and of plans thwarted.* You must at all times retain your ambition, but not that 'vaulting ambition which o'erleaps itself.' Ambition must be controlled just as if you are to reach the highest class at a game like tennis, you must learn to control your speed. And if disappointment comes—and it is bound to come—remember that it should be taken as a stimulant and never as a discouragement. The other side of an emergency is always an opportunity.

My father-in-law, Lord Cahir, used to keep pasted into a drawer of his desk the following quotation from Robert Louis Stevenson: 'The conditions of conquest are easy: we have but to toil a while, endure a while, believe always and never turn back.' A motto which served him well may serve you also.

6. *Be hard-headed but not 'hard-boiled.'* The most valuable asset in any business is judgment. You must learn to be an optimist in adversity and to practise caution in times of prosperity. You must learn when to go forward and when to halt, when to be firm and when to be conciliatory. Someone once asked one of the Rothschilds how he accumulated such a fortune, and he replied by saying: 'By always selling out too soon.' He had learnt that you can never expect to sell that you have got to sell at the top of the market, and if you try to, you will find that others have decided to sell before you and that the market has fallen away. Fortunes are lost by those who get swept away in a flood of popular optimism or pessimism: they are made by those who can coolly and calmly judge when the popular opinion is wrong.

Judgment is not learnt from books, it is learnt by observation and analysis of the world around you. You should at all times be asking yourself such questions as 'What is the reason for this?'—'Can I do that better than it is being done already?' and so on. The answers to these sorts of questions do not lie in books but in your own powers of close observation and your own balanced judgment. Use your brain in close conjunction with your eyes.

7. *Do not spare yourself, but do not become a machine. Whatever your ideals are, keep them. They are an asset of true value.* One of the greatest assets which you can possess in business is self-reliance. You must be prepared, as the Finance Member for Bengal was saying to the students of the

Commercial Institute the other day, to assume and discharge responsibilities. You must give up seeking a job that carries the least trouble and the least risk. In fact I would go further and say that the people of Bengal must be prepared to incur greater risks if they are to hold their own with other communities in the business world. The obsession for landed property is a mistake, and the system of land tenure which allows too many people to eke out a living without the need to work or venture, has been the bane of business in Bengal. It is undoubtedly a fact that many a family business in Bengal has been abandoned because of the risk, and until those who have the power and the money are prepared to take more risk, business must stagnate. All business is a venture, and in business risk is unavoidable, for, as Dr Johnson said: 'nothing will ever be attempted if all possible objections must be overcome first.' The man who succeeds is the man who sums up the risks with the greatest ability and makes the fewest mistakes. No business man ever succeeded without making some mistakes: it is from them that he learns.

8. *Take an interest in public affairs. Protect from demagogic assault the things which by test and trial have been found worthy of preservation.* Never accept anything just because you are told of it. Be careful to avoid the attractive slogans of people who would be thought to offer you an easy millenium. Their remedy for the ills of the world are so often meretricious. Think for yourself, estimate in your own mind what things in your daily life are good at heart and worthy of preservation, and be prepared to work for them. And never accept a statement without personally analysing it. As soon as you can say what you think, and not what some other person has thought for you, you are on the way to becoming a remarkable man.

9. *Meet your fellow-men with confidence. Scepticism and mistrust beget aggression. Confidence begets goodwill.* A sense of co-operation and of loyalty will be two of your biggest assets in a business career. It is very easy to be selfish in business but there is no real need for a selfish policy. Measure your success by the work done, not by the money you have made at the expense of others.

And you will forgive me for saying that one of the biggest reasons which prevents progress in the Bengal business world is the lack of co-operation between different interests. I make no apology for stressing this point, because it has already been made by Sir P. C. Ray in his first address. 'You will have seen recently the value of co-operation among the managing agents of the jute mills. For some years this has been lacking, but the moment co-operation returned to the industry, as if by magic the trade has taken a turn for the good of all. Some of this spirit is needed in many other trades today, notably in the coal trade. It was said by one of the greatest organisers of business in Pre-War Germany that he made it a principle never to tie an unwilling partner to an agreement which

the latter considered to be detrimental to his vital interests, and he would only approve of an agreement if both parties felt satisfied that they had done a good stroke of business by concluding it. That is well worth bearing in mind, and you will find over and over again by experience in the business world that a lean compromise is better than a fat law-suit.

And remember that all joint-stock enterprise is based upon co-operation and trust. In the early stages of business development a few people who trusted each other came together to pool their resources in a partnership. Joint-stock companies are mainly an extension of that, and for their success trust is necessary. The shareholders must trust the management and direction, and those, who are responsible for the management and direction, must above all earn the trust of their shareholders. If Bengal is to advance in the business world, you must do much more to pool your resources and to trust your own business leaders who have earned your confidence. To you who have a business career in mind an immense field lies open in the development of joint-stock enterprise on these lines, but the prime necessity is mutual confidence.

10. *Like everything worth having in life, success has to be paid for by assuming and discharging responsibilities.* I have already touched upon the lessons of this maxim in my remarks above, but remember this that most problems of trade are settled by the exercise of personal courage and imagination. You should never be satisfied with a cheap success, and if you meet with a real success, remember to keep your head. Some people grow under responsibility, others merely swell, and the moment you estimate your success at more than it is worth, you have taken the first step backwards.

Those were the maxims of great leader. You will not be able to carry them all in your minds, but I understand that some part at any rate of these addresses are being reprinted, and if you will study these maxims—maxims which apply anywhere in the world—perhaps they may help you a little hereafter in your business careers.

Test Questions.

1. ✓ What are the essential requisites for the success of a business? *(All. B. Com. 1939)*
2. How far would you consider a theoretical training as necessary and sufficient for success in a practical business career? *(Bombay B. Com. 1942)*
3. What in your opinion are the requisites of a successful business man? *(Bombay B. Com 1945)*
4. "Honesty is the best policy even in business." Discuss. *(Bombay B. Com. 1914)*

CHAPTER 2

NATURE AND CONSTITUTION OF BUSINESS HOUSES

In this and the following chapters, we propose to examine the nature and constitution of business houses. All business concerns are either proprietary or joint stock in form. A proprietary business is one in which the capital is furnished by the proprietor or proprietors and which is also managed by them. A joint stock concern, on the other hand, is one in which the capital is usually supplied by the public, but whose management is in charge of the proprietors' representatives known as directors and managing agents. A proprietary business may be the property of one person or several persons. Where only a single individual is the owner of a business, he is called the sole trader; but a business owned by several persons is known as a partnership. So there are really three principal types of business houses: sole trader, partnership and joint stock company.

1. Sole Trader

Where the ownership of a business rests in a single person there is little to be said on the constitution of its proprietorship. There is no legal formality to be observed in setting up such a business. The owner should, of course, have the capacity to contract, or his trading contracts will not be enforceable in a court of law. The sole trader has to supply all the capital needed for the business and he himself has to look after its management with the help of paid employees, if necessary. All the profits of the business belong to him and he must bear all the losses. He is responsible with all that he possesses—whether invested in his business or not—for all debts incurred either private or on account of his business.

The sole trader is specially interesting because of his potentialities. Many of our large businesses, now conducted under other forms of proprietorship, have grown out of individual enterprise. A highly capable or successful sole trader soon reaches the limit of his individual means and has to press into his service the financial help and managing ability of others. The proprietorship of his business probably passes through the partnership into the company form.

Advantages. The individual enterprise has several marked advantages which make it a prominent type of business organisation. These are ;—

1. A sole trader can ordinarily undertake any kind of business enterprise except those that are carried on by the Government exclusively (e. g., the manufacture of opium) or those that require special licenses (e. g., the generation and supply of electricity) or those that are forbidden on grounds of public policy. He may continue his business as long as he likes and may retire from it at any time. The fact that a sole trader may start a business without any formality and may retire in the same way promotes business enterprise.

2. As an individual proprietor receives all the profits which are made in his business, he has a great incentive for hard work. He takes the greatest possible interest in the business and this leads to efficient and economical management.

3. A sole trader, having no one else to consult, can act in all emergencies with greater promptness. He may thus take advantage of business opportunities that are impossible in the case of partnerships or companies. For the same reason he may avoid certain dangers that ordinarily surround and sometimes destroy business enterprises. Of course, the ability to act promptly is not an unmixed business blessing. It is often the case that hasty action is the direct cause of business failure.

4. A sole trader can keep his own affairs to himself. The more the competitors know of one's business plans and processes, the less the chances of ultimate success.

5. Since every business enterprise has its own peculiar risks, its owner must be able to manage it properly; otherwise the business will fail. A sole trader has, therefore, an opportunity of learning the art of efficient business management.

Disadvantages. There are, however, several particulars in which the individual enterprise fails to provide successful business organisation, and these are:—

1. A sole trader cannot supply all the capital needed for an expanding business. Except where the business prospers to an unusual degree and where the owner is willing to leave a large portion of the profits in the business, individual enterprise may seriously hamper growth. At best, expansion of capital by means of undrawn profits is a slow process, and may often be too slow to allow normal development to take place.

2. Large businesses often require business judgment, skill and ability beyond the capacity of any one man to furnish; hence several men enter into a combination to conduct a business enterprise jointly in order that they may secure the benefits of their co-operative wisdom.

3. A sole trader carries the whole risk of loss on his own shoulders, and this sometimes leads to his complete ruin. Business men hesitate to put all their eggs in one basket and undertake the risks that follow from such a policy. Moreover a person cannot avoid the risks by organising and managing several small

severally for the debts incurred by or on behalf of the firm in the ordinary course of business ; in fact, to this extent, each partner is an agent of and for the others.

Need for Partnership. Every business, if it is to be a success, must possess certain requisites. Its owner must be able to supply the necessary capital ; he must have business ability and devote sufficient time to its affairs, and he must also command some connection or influence in order to attract customers. It may be said that if a business is started with adequate capital and business ability on the part of its proprietor, it will automatically acquire connection in course of time. That is true, but it will take time. It is, however, very helpful if the proprietor of a new business already possesses some influence with the likely clients. If the business is a small one, all these requisities may be furnished by a single individual, but when the business grows and needs more than ordinary quantity of capital, business ability and influence, it may be that its sole proprietor cannot himself contribute them. In order that the proprietors themselves may possess the various qualities required for success, we have frequently to resort to combination, so that the qualities possessed by several individual may be made collectively available for the common purpose. Hence the need for partnership arises owing to the inequality of gifts held by different persons. An individual may have business ability and connection but may not be fortunate to command sufficient capital, or a man may possess enough capital but may have no ability and influence. When people with different gifts combine their resources for a common purpose and form a partnership, they all stand to gain or lose together, and therefore their interests become identical.

If an individual has business ability and some connection but is short of capital, it may be that he can secure the necessary funds by borrowing from others instead of taking a moneyed man into partnership. But to carry on business with other people's money is dangerous. In the first place, high interest has often to be paid to lenders, secondly, the lenders have the right to demand back their money at any time which may not be in the best interests of the business, thirdly, the payment of interest does not depend upon profits being earned and has to be paid whether the business is making profits or is running at a loss ; and finally, a business run entirely with borrowed money cannot win the confidence of its customers.

If a person commands capital but does not possess the necessary ability and connection, it may be said that he can hire both talent and influence. It is possible to do so, but it will not be a satisfactory arrangement in all cases. A skilled manager may be employed for running the business, but it depends upon the nature of the business how far it would be safe to do so. As reinforcing the strength of the proprietor, an experienced employee is certainly an advantage ; but if all the skill is to be in the hands of employees, the business cannot have a chance for permanent success. The employee may go away at any time if he is offered better terms by a competitor, or the employee may be tempted to set up a competitive business himself. In order to avoid the risk of possible competition

benefit of all. One partner may furnish the major part of capital, another may place his business ability and experience at the disposal of the firm, a third may devote the whole of his time and attention to its business, and a fourth may use his influence for the common purpose. Thus by a proper blending of the different gifts the business of the firm can be run smoothly and successfully.

It is equally necessary for a good partnership that all the partners must have mutual trust and confidence, and this mainly depends upon the right selection of partners. At the time persons become partners, they are generally in good spirits, but later on, unless each completely trusts the other, there may be many occasions for quarrel and dispute amongst them. Many of the greatest successes of commerce have resulted from the partnership of two or more men who know exactly how to supplement each other and to take their own full share in responsibility. On the other hand, some of the greatest failures of business have resulted from partnerships. There have been cases where men, who in other circumstances, would have done well, by trying to pull together in double harness have merely impeded each other. Possibly when people enter into partnership, the first thing they should realise is temperament. There are some men who are entirely unable to be partners in any satisfactory manner. These include the autocrats, who only understand doing things in their own way but who brook no interference from any one else. But more generally the secretive type of man is the bad partner. One can obey or one can command a secretive person, but one cannot work on even terms with him, for when the habit is ingrained, the lack of frankness and confidence will certainly lead to difficulties. Ideal partners are those who esteem each other and work well together. Nearly always when partnerships prove unsatisfactory it is because the partners have not learnt enough about each other before linking their commercial fates together. Employees who are admitted as partners do not sometimes prove to be good partners, because they cannot or will not contribute the share a partner should—not of work but of creative management. Just as there are persons who always have the master spirit wherever they are, so also there are others who cannot acquire the master spirit. They are employees by nature, and can only see things in that way. Such men are usually most unsatisfactory partners, especially when there are difficult problems of finance and policy to be faced. Moreover, the man who regards the change from being employed to becoming a partner as a change from hard work to easy work is usually a most undesirable partner.

A good partnership must extend over a long period of time during which each partner must work for the common good without giving a second thought to his own personal interest, as opposed to the interests of his firm. If a partner is not working for the firm, he is working against it, and the result is bound to be very unsatisfactory. According to law, each partner can bind his co-partners by his acts done in the ordinary course of the firm's business. Sheer careless,

The minority interest in a partnership is adequately protected by law. A dissatisfied partner may *withdraw and dissolve the firm*, or if that be undesirable he may so hamper its affairs as to force his co-partners to buy him out.

Disadvantages. As the number of partners is limited to twenty, the amount of capital which can be raised by a firm is also limited; and in the absence of limited liability, investors who have not the capacity or the desire to participate in management cannot afford to enter a partnership. Not only this but a share in a partnership business can be transferred with such difficulty that it does not appeal to many investors. Such a share can only be sold to a co-partner or to a stranger with the consent of all the co-partners, a condition which so limits the market that it may often have to be sold at a sacrifice. Further after the sale of his share an outgoing partner remains liable for debts to creditors whose claims were incurred prior to his withdrawal unless the creditors agreed to exempt him, and to other creditors unless constructive notice has been given regarding his withdrawal from the business.

The liability of individual partners may be regarded as excessive in many cases. When the business unit needed only a small amount of capital and business relations were very personal, the heavy personal liability for the firm's obligations was not so burdensome, and probably did good service in making possible wider business dealings. But now that trade and commerce are generally carried on on a large scale and require vast capital and extensive credit operations, the personal liability of partners may be increased beyond all reasonable limits. The larger the number of partners, the larger the scale of business, the greater the partners' personal liability.

A partnership is liable to dissolution at any time by the death, insolvency or lunacy of a partner; and a well established business may suddenly come to an unexpected end.

A partnership often lacks prompt and united management. Too many cooks may spoil the business broth. If the partners seek to meet this difficulty by delegating management to one of their number they soon realise that their unlimited liability will not allow them to do so. The management can work well if the partners act in harmony and honestly; but too often this is not the case. Among a large number of persons there is almost sure to be at least one who would develop dishonest traits or prove unwise, and whose action would involve all the members in unfortunate complications. In short a serious problem in partnership organisation is to secure harmony of interests in management.

Partnership Agreement. An agreement is an essential ingredient to a contract of partnership. It may be either express or implied. An implied agreement may be inferred from the course of dealings. The agreement of partnership need not be in writing; but if it is in writing it must be stamped, and if it relates to or creates or involves rights to immovable property, it must also be registered. A partnership contract may be oral, but it is always safe to have a written agreement. A partnership agreement, if it is to deal with all the matters

affect the partners only. In pursuance of this idea, a number of sections in the Act are "subject to contract between the partners", that is to say, they contain rules which are applicable in the absence of contract varying them.

Definition of Partnership. Partnership is the relation between persons, who have agreed to share the profits of a business carried on by all or any of them acting for all. Persons who have entered into partnership with one another are called individually "partners" and collectively "a firm", and the name under which their business is carried on is called the "firm name" (Section 4).

Where no provision is made by contract between the partners for the duration of their partnership, the partnership is "partnership at will," (Section 7). A person may become a partner with another person in particular adventures or undertakings. Such a partnership is called particular partnership (Section 8).

Elements of Partnership. The definition of partnership contains the following three distinct elements:—

1. There must be an agreement entered into by all the persons concerned. This means that partnership can arise only as a result of an agreement, express or implied, between two or more persons. There must be an agreement entered into by all the partners. The persons may be natural or legal. A limited company or a joint Hindu family can be a partner, but no partnership can be formed consisting of more than ten persons for the purpose of carrying on the business of banking, or of more than twenty persons for the purpose of carrying on any other business having for its object the acquisition of gain. Partnership is thus created by a contract, it does not arise by the operation of law. The contract which is the foundation of partnership must possess the necessary attributes of contracts, i. e., it must be for a lawful object and between competent persons.

2. The agreement must be to share the profits of a business. The object of the agreement must be to carry on a business, and the business must be legal. The sharing of profits is an essential element of a partnership agreement. The members of religious or charitable societies and clubs are not partners, as there is no idea of sharing or even making profits in these associations. The agreement to share profits is essential, but an agreement to share the losses is not essential. Where nothing is said as to the sharing of losses, it is implied in a partnership agreement. It may, however, be agreed, that as between the partners any one or more of them shall not be liable for losses.

3. The business must be carried on by all or by any of the persons concerned acting for all. This means that every partner is in contemplation of law, the agent of the partnership and may consequently bind all the other partners by his acts in all matters within the scope and objects of partnership. In fact, the relation of principal and agent amongst the partners, mutual agency, is the true test of partnership.

How Existence of Partnership Determined. It is often important to ascertain whether a partnership exists in a particular case or not. This may

be necessary to determine the rights of the parties between themselves or to enable the creditors to know by whom the payment of their debts is to be made.

The main rule to be observed in determining the existence a partnership is that regard must be paid to the true content and intention of the parties as appearing from the whole facts of the case. All the facts must be considered together. The mere fact that the parties call themselves partners in the agreement does not constitute a partnership.

The relation of partnership arises from contract and not from status. Therefore the members of a joint Hindu family carrying on a family business or a Burmese Buddhist husband and wife carrying on a business are not partners in such business (Section 5). A joint Hindu family firm is not a result of an agreement voluntarily entered into by persons, it arises by the operation of law. The moment a child is born into the trading family, by the mere fact of its birth, it becomes a member of the trading firm. As partnership springs from contract and not out of status, it follows that the joint Hindu family firm is not partnership. Under Mohammadan law there is no family trading partnership such as exists under Hindu Law, and any partnership transaction between two Mohammadan brothers must be governed by the contract between them.

The sharing of profits or of gross returns arising from a property by persons holding a joint or common interest in that property does not, of itself, make such persons partners.

The receipt by a person of a share of the profits of a business, or of a payment contingent upon the earning of profits or varying with the profits earned by a business does not of itself make him a partner with the persons carrying on the business. For example, the receipt of such share or payment by the following persons does not of itself make the receiver a partner with the persons carrying on the business :—

- (a) By a lender of money to persons engaged or about to engage in any business,
- (b) By a servant or agent as remuneration,
- (c) By the widow or child of a deceased partner as annuity; or
- (d) By a previous owner or part owner of the business as consideration for the sale of the goodwill or share thereof (Section 6).

Joint Hindu Family Business. A joint Hindu family may carry on a family business exclusively for its own benefit, or it may carry on a business with one or more outsiders as partners with the family. A joint Hindu family carrying on a family business may have some of the characteristics of a firm, but it is not a firm. The partnership law does not apply to a joint Hindu family business, which is governed entirely by Hindu Law.

Distinction Between Partnership and Joint Hindu Family Firm. The principal points of distinction between partnership and joint Hindu family firm are as follows :—

1. A partnership is created by contract, but a joint Hindu family firm is created by the operation of Hindu Law.

2. In a partnership every partner is an agent of the firm and has implied authority to bind the firm by his acts done in the ordinary course of business : but in a joint Hindu family firm the managing member or *karta* alone can pledge the credit or property of the family for the purpose of the business.

3. In a partnership the share of a partner in the partnership property as well as his own separate property is liable for the payment of the partnership debts. But in a joint Hindu family firm only the managing member is personally liable, and the other members are liable only to the extent of their shares in the family property, their separate properties not being liable.

4. A partner is always entitled to call for an account and examine the account books himself ; but a member of a joint Hindu family (known as a co-parcener) is not entitled to call for an account for the past profits and losses while severing his connection with the family business except in some special cases.

5. Subject to contract between the partners, a partnership is dissolved by the death of a partner. The death of a co-parcener or even the managing member does not dissolve a joint Hindu family firm.

6. In a partnership a minor cannot become a partner though he may be admitted to the benefits of partnership : but in a joint Hindu family firm a minor becomes a co-parcener.

7. A partnership is required to be registered in order to maintain suits against partners or outsiders, but no such registration is necessary in the case of a joint Hindu family firm.

Relations of Partners to one Another.

Partners are bound to carry on the business of the firm to the greatest common advantage, to be just and faithful to each other, and to render true accounts and full information of all things affecting the firm to any partner or to his legal representative. Every partner shall indemnify the firm for any loss caused to it by his fraud in the conduct of the business of the firm (Sections 9 and 10). These provisions are absolute and are not subject to contract between the partners. But other mutual rights and duties of partners, whether stated in a partnership agreement or defined by the Act, may be varied by the consent of all the partners, and such consent may be given expressly or be inferred from a course of dealing. Such contract may provide that a partner shall not carry on any business other than that of the firm while he is a partner (Section 11).

The Act contains important rules declaring the rights and duties of the partners. Under sections 12-17, subject to any contract between the partners, their mutual relations are governed by the following rules :—

1. Every partner has a right to take part in the conduct of the business.

2. Every partner is bound to attend diligently to his duties in the conduct of the business.

3. Any difference arising as to ordinary matters connected with the business may be decided by a majority of the partners, and every partner has a right to express his opinion before the matter is decided; but no change can be made in the nature of the business without the consent of all the partners.
4. Every partner has a right to have access to and to inspect and copy any of the books of the firm.
5. A partner is not entitled to receive remuneration for taking part in the conduct of the business.
6. The partners are entitled to share equally in the profits earned, and must contribute equally to the losses sustained by the firm.
7. Where a partner is entitled to interest on his capital, such interest is payable only out of profits.
8. A partner, making for the purposes of the business any payment or advance beyond the amount of capital he has agreed to subscribe is entitled to interest thereon at the rate of six per cent. per annum.
9. A firm must indemnify a partner in respect of payments made and liabilities incurred by him in the ordinary and proper conduct of the business and in exercising any emergency power for protecting the firm from loss.
10. A partner must indemnify the firm for any loss caused to it by his willful neglect in the conduct of the business of the firm.
11. All the property of the firm including goodwill is to be held and used by the partners exclusively for the purposes of the business.
12. If a partner makes any secret profit out of the firm, he must account for that profit and pay it to the firm.
13. If a partner carries on any business competing with that of the firm, he must account for and pay to the firm all profits made by him in that business.
14. Where a change occurs in the constitution of a firm, the mutual rights and duties of the partners in the reconstituted firm remain the same as they were immediately before the change, as far as may be.
15. Where a firm constituted for a fixed term continues to carry on business after the expiry of that term, the mutual rights and duties of the partners remain the same as they were before the expiry.

Agreement Between Partners in Restraint of Trade. Section 27 of the Indian Contract Act lays down that an agreement in restraint of trade is void. The general rule is that every agreement by which one is restrained from exercising a lawful profession, trade or business of any kind, is to that extent, void. In the case of a partnership, there are, however, four exceptions to this general rule, and these are :—

will. Consequently, even when a partner transfers his interest in a firm, the transferor does not cease to be a partner nor does the transferee become one.

During the continuance of the partnership, the transferee of a partner's interest is not entitled to interfere in the conduct of the business, or require accounts, or inspect the books of the firm. He is entitled only to receive the share of profits of the transferring partner and must accept the account of profits agreed to by the partners.

But if the firm is dissolved or if the transferring partner ceases to be a partner, the transferee is entitled to receive the transferring partner's share of the assets of the firm, and, for this purpose, is entitled to an account as from the date of dissolution (Section 29).

Minor as Partner. Since capacity to contract is essential for the formation of partnership, a minor cannot become a partner himself so as to acquire rights and be subject to the liabilities of a partner. He can however, be admitted to the benefits of a partnership by an agreement executed by his guardian on his behalf with the partners. The provisions of law in this respect are as follows :—

1. A minor cannot be a partner in a firm, but he can be admitted to the benefits of partnership. He can be given this footing in the firm only by the express consent of the partners, but he cannot be thrust upon them.

2. A minor has a right to such share of the property and of the profits of the firm as may be agreed upon, and he may have access to and copy any of the accounts of the firm. He is allowed access only to accounts, and not to books, because it is dangerous to give the minor access to all the books of the firm, as some of the books may contain secrets which should be restricted to the partners. He cannot sue the partners for his share of the property or profits except when he severs his connection with the firm. Only his share of property and profits in the firm is liable for the acts of the firm, but he is not personally liable so long as he is a minor.

3. At any time within six months of his attaining majority or of his obtaining knowledge that he had been admitted to the benefits of partnership, whichever date is later, a minor may give public notice that he wants to become a partner in the firm or to sever his connection with it; but if he does not give any public notice, he becomes a partner in the firm on the expiry of the said six months.

4. When a minor becomes a partner, his rights and liabilities as minor continue up to the date on which he becomes a partner, but he also becomes personally liable to third parties for all the acts of the firm done since he was admitted to the benefits of partnership; and his share in the property and profits of the firm shall be the share to which he was entitled as a minor.

5. When a minor gives public notice not to become a partner, his rights and liabilities continue to be those of a minor up to the date on which he gives public notice, his share is not liable for any acts of the firm done after the date

of the notice, and he becomes entitled to sue the partners for his share of the property and profits (Section 30).

Incoming Partners.

Subject to contract between the partners, no person can be introduced as a partner into a firm without the consent of all the existing partners. The general idea is that the consent of all existing partners is required to the introduction of a new partner in order that the firm may work harmoniously. However, if a previous contract has been made by the partners to the effect, for example, that the senior partner shall have the right of introducing a new partner at any time or juncture, the contract will be binding on the partners, even though when the time comes or the juncture arises, one or more of the partners may be unwilling to accept the new partner—Section 31 (1).

Rights and Liabilities. The following are the rights and liabilities of an incoming partner:—

1. A new partner is not liable for any acts of the firm done before he became a partner—Section 31 (2). He becomes liable for all the acts of the firm done after he becomes a partner (Section 25).

2. When a minor, who has been admitted to the benefits of partnership, chooses on attaining majority to become a partner, his liability relates back to the date on which he was admitted to the benefits of partnership (Section 30).

3. An incoming partner is subject to the terms of the partnership except as varied by express agreement; and he is entitled to all the rights of the existing partners except as varied by express agreement.

Outgoing Partners.

A partner becomes an outgoing partner by retirement, expulsion, insolvency or death.

Retirement. A partner may retire (a) with the consent of all the other partners; or (b) in accordance with an express agreement by the partners; or (c) where the partnership is at will, by giving notice in writing to all the other partners of his intention to retire—Section 32 (1).

A retiring partner may be discharged from any liability to a third party for acts of the firm done before his retirement by an express or implied agreement made by him with such third party and the partners of the reconstituted firm—Section 32 (2). A retired partner remains liable to third parties for all acts of the firm until he gives public notice of retirement, but a retired partner is not liable to a third party who deals with the firm without knowing that he was a partner—Section 32 (3). A dormant partner may retire from a firm without giving notice to the world.

Expulsion. A partner cannot be expelled from a firm by any majority of the partners, save in the exercise in good faith of power conferred by contract between the partners—Section 33 (1). A power to expel a partner can only be conferred by an express agreement between the partners. Even when such a power exists, it can only be exercised by a majority of the partners and it must

be exercised in the utmost good faith.

Section 33 (2) provides that the rules which govern the liability of a retired partner to third parties will apply in the case of an expelled partner.

Insolvency of a Partner. Where a partner in a firm is adjudicated insolvent, he ceases to be a partner on the date on which the order of adjudication is made, whether or not the firm is thereby dissolved. Where under a contract between the partners the firm is not dissolved by the adjudication of a partner as an insolvent, the estate of a partner so adjudicated is not liable for any acts of the firm and the firm is not liable for any act of the insolvent, done after the date on which the order of adjudication is made (Section 34).

Deceased Partner. Where under a contract between the partners, the firm is not dissolved by the death of a partner, the estate of a deceased partner is not liable for any act of the firm done after his death—Section 35. Subject to contract between the partners, a firm is dissolved by the death of a partner—Section 42 (c). Where a firm is thus dissolved, though the surviving partners continue to be liable for acts done on behalf of the firm until public notice of dissolution is given, the estate of the deceased partner is not subject to any such liability—Section 45 (1). It means, therefore, that the estate of a deceased partner is not liable for any act of the firm done after his death, whether the death has dissolved the firm or not.

Rights and Liabilities. The following are the rights and liabilities of an outgoing partner :—

1. A retired or expelled partner may be discharged from any liability to any third party for acts of the firm done before his retirement or expulsion by an express or implied agreement made by him with such third parties and the partners of the reconstituted firm—Section 32 (2).

2. A retired or expelled partner will be liable to third parties for all acts of the firm, until he gives public notice of retirement or expulsion; but he will not be liable to a third party who deals with the firm without knowing that he was a partner—Section 32 (3).

3. An outgoing partner has the right to carry on a business competing with that of the firm and to advertise such business except where he has agreed with the firm not to carry on such business within specified local limits—Section 36.

4. An outgoing partner has no right (a) to use the firm's name, (b) to represent himself as carrying on the business of the firm, or (c) to solicit the custom of the old customers of the firm, unless the other partners have contracted themselves out of their rights in this respect—Section 36.

5. Where the continuing partners carry on the business of the firm with the property of the firm without any final settlement of accounts as between them and the outgoing partner, then in the absence of a contract to the contrary, the outgoing partner is entitled to claim a share in the profits of the firm, or at his option an interest at 6 per cent. per annum—Section 37.

Dissolution of a Firm

The dissolution of partnership between all the partners of a firm is called the dissolution of the firm (Section 39). The following are the five ways in which a firm may be dissolved :—

Dissolution by Agreement. A firm may be dissolved with the consent of all the partners or in accordance with the contract between the partners (Section 40).

2. **Compulsory Dissolution.** A firm is dissolved (i) by the adjudication of all the partners or of all the partners but one as insolvent, or (ii) by the happening of any event which makes it unlawful for the business of the firm to be carried on or for the partners to carry it on in partnership (Section 41).

3. **Contingent Dissolution.** Subject to contract between the partners, a firm is dissolved (i) if constituted for a fixed term, by the expiry of that term; (ii) if constituted to carry out one or more adventures or undertakings, by the completion thereof; (iii) by the death of a partner, and (iv) by the adjudication of a partner as an insolvent (Section 42).

4. **Dissolution by Notice.** Where a partnership is at will, the firm may be dissolved by any partner giving notice in writing to all the other partners of his intention to dissolve the firm, and the firm is dissolved as from the date mentioned in the notice as the date of dissolution or, if no date is so mentioned, as from the date of the communication of the notice (Section 43).

5. **Dissolution by Court.** At the suit of partner, the Court may order the dissolution of a firm on any of the following grounds, viz.—

- (i) That a partner has become of unsound mind,
- (ii) That a partner, other than the partner suing, has become in any way permanently incapable of performing his duties as partner,
- (iii) That a partner, other than the partner suing, is guilty of conduct which is likely to affect prejudicially the carrying on of the business;
- (iv) That a partner other than the partner suing, wilfully or persistently commits breach of agreement relating to the management of the affairs of the firm or the conduct of its business, or otherwise so conducts himself in matters relating to the business that it is not reasonably practicable for the other partners to carry on the business in partnership with him,
- (v) That a partner, other than the partner suing, has transferred the whole or his interest in the firm to a third party, or allowed his share to be charged or sold by the Court,
- (vi) That the business of the firm cannot be carried on save at a loss, or
- (vii) On any other ground which renders it just and equitable that the firm should be dissolved (Section 44).

Conduct of Winding up. The partners are the proper persons to take charge of the assets and wind up the affairs of the firm, and their power to bind

the firm continues for this purpose notwithstanding dissolution (Section 47). If after dissolution they cannot agree as to the winding up, the Court will appoint a receiver and, if necessary, a manager, and will, if necessary, restrain a partner by injunction from doing any act which will impede the winding up. Where a partnership is dissolved by the death or insolvency of a partner, the continuing or solvent partners are entitled to wind up the affairs.

In settling the accounts of a firm after dissolution, the goodwill shall, subject to contract between the partners, be included in the assets, and it may be sold either separately or along with other property of the firm; and any partner may, upon the sale of the goodwill of the firm, make an agreement with the buyer that such partner will not carry on any business similar to that of the firm for a specified period or within specified local limits, and such an agreement is valid if the restrictions imposed are reasonable.

Subject to agreement by the partners, the accounts of a firm on dissolution must be settled according to the following rules :—

1. Losses, including deficiencies of capital, shall be paid first out of profits, next out of capital, and, lastly, if necessary, by the partners individually in the proportions in which they were entitled to share profits.

2. The assets of the firm, including any sums contributed by the partners to make up deficiencies of capital, shall be applied in the following order :—

(a) in paying the debts of the firm to third parties;

(b) in paying to each partner rateably what is due to him from the firm for advances as distinguished from capital;

(c) in paying to each partner rateably what is due to him on account of capital; and

(d) the residue, if any, shall be divided among the partners in the proportions in which they were entitled to share profits (Section 48).

Where there are joint debts due from the partnership and also separate debts due from any partner, the partnership property must be first applied in payment of the debts of the firm, and if there is any surplus then the share of each partner in such surplus must be applied in payment of his separate debts or paid over to him if he has no debts. So also the separate property of any partner must be first applied in payment of his separate debts, and the surplus, if any, in payment of the debts of the firm (Section 49).

Right to Return of Premium Where a partner has paid a premium on entering into partnership for a fixed term, and the firm is dissolved before the expiration of that term otherwise than by the death of a partner, he shall be entitled to repayment of the premium (or of such part thereof as may be reasonable) regard being had to the terms on which he became a partner and to the length of time during which he was a partner, unless :—

(a) the dissolution is mainly due to his own misconduct, or

(b) the dissolution is in pursuance of an agreement containing no provision for the return of the premium or any part of it (Section 51).

1. Unless the firm is registered and the person suing is or has been shown in the Register of Firms as a partner of the firm, he or his nominee or agent cannot bring a suit to enforce a right arising from a contract or conferred by law against the firm or against any past or present partner of the firm.

2. No suit to enforce a right arising from a contract can be instituted by or on behalf of a firm against any third party unless the firm is registered.

3. The same disabilities also apply to a claim of set-off or other proceeding to enforce a right arising from a contract.

The non-registration of a firm does not, however, affect the following rights :—

1. The right of third parties to sue the firm or any partner.
2. The right of a putnam to sue for dissolution of a firm or for accounts of a dissolved firm, or to enforce any right or power to realise the property of a dissolved firm.
3. The power of an official assignee or receiver to realise the property of an insolvent partner.
4. The rights of firms or partners in firms having no place of business in British India.
5. Any suit or set-off in which the claim does not exceed Rs. 100 (Section 69).

Advantages of Registration. Registration lies entirely within the discretion of the firm or a partner concerned : but the firm and its creditors and partners stand to gain from registration in the following ways :—

1. *Firm.* An unregistered firm cannot enforce its claims against third parties in the civil courts, and any partner who is not registered cannot enforce his claims either against third parties or against his fellow partners. There is one important exception to this disability, namely, an unregistered partner may sue for the dissolution of a firm. This exception is made on the principle that registration is designed primarily to protect third parties, and the absence of registration need not prevent the disappearance of an unregistered firm.

2. *Creditors.* Once registration has been effected, the statements recorded in the Register of Firms regarding the constitution of the firm will be conclusive proof of the fact therein contained against the partners making them, and no partner whose name is on the Register will be permitted to deny that he is a partner. This should afford a strong protection to persons dealing with the firm against false denials of partnership for the evasion of liability by the substantial members of a firm.

3. *Incoming Partners.* As regards a partner newly introduced into a firm, if he fails to register he will incur a grave risk of being unable to claim his dues from his partners, and will have to rely solely on their good faith or sue for dissolution.

4. *Outgoing Partners.* As regards outgoing partners, the estate of a deceased partner or of an insolvent partner is in no case liable for the acts of

The principle of complete freedom to conduct business enterprise under the company form of organisation has now been established for a long time. It really amounts to a group of business people saying: "We propose to form a business association with a capital of say) Rs. 1,00,000. We announce beforehand that this is the amount of capital at stake and that our liability is restricted to this total. We invite people to associate themselves with us in this enterprise and we shall invite other people to trade with us on these terms. We shall *compel no one to join with us or to remain with us; we shall compel no one to trade with us.* We are prepared to submit to a certain amount of statutory regulation designed to prevent fraud and other irregularities, regulation applicable to any form of business, but we shall certainly not submit without the strongest protest to any particular or discriminating regulation aimed at our special form of organisation. We are a private enterprise organised in a way convenient to ourselves, and in a democracy and a system of private enterprise we have an absolute right to suit our own convenience in the matter."

The joint stock enterprise in India is not indigenous but exotic. It is not a natural growth of our old forms of business organisation, but it has been imported from England like so many other good things. In England the formation of joint stock companies for trading and other purposes dates back for several centuries. The East India Company was founded in 1600, the Hudson Bay Company in 1670, and the Bank of England in 1694, all under royal charters granted by the Crown. Later on some companies were formed by special Acts of Parliament. Up to 1844 companies could only be incorporated either by royal charter or by special Acts of Parliament. But in 1844 a decisive advance was made and the Joint Stock Companies Registration Act was passed. This was the first Act which provided for incorporation by mere registration; and for the first time commercial combinations obtained the advantages of incorporation without the necessity of a royal charter or a special Act of Parliament. The privilege of limited liability was not, however, granted till 1855. The present company law in England is contained in the English Companies Act, 1948.

The limited liability feature possessed by joint stock companies is one of the reasons why state regulation of companies is needed. The interests of the creditors must be given some degree of protection, though it may curtail the freedom of action on the part of the owners.

In India the joint stock form of business organisation came from England and so did the company law. Thus whenever any legislation was enacted in England, it was sooner or later adopted in this country. Following the English Companies Act of 1844, the Joint Stock Companies Act of 1850 was passed here, and it was the first Act under which companies could be registered. This Act was the basis on which subsequent Acts were founded. The Supreme Courts of Calcutta, Bombay and Madras were authorised to order the registration of companies under this Act. A number of companies were registered between 1850 and 1857, and of these the Bengal Coal Company is still in existence.

and debentures of small denomination make it possible for investors to diversify their investments and thus reduce the risks of loss to a minimum. Even so small a sum as Rs. 1,000 may be invested in a number of different companies.

Further, the device of issuing both shares and debentures serves to attract the funds of people of different temperaments and of different economic positions. Debentures, which have first claim upon the company's earnings, make their appeal to those who are conservative or whose economic position is such as to make safety of investment the first requisite. On the other hand, shares offer an opportunity of higher returns and thus appeal to people who are willing to take chances in the hope of large rewards and to those whose economic position is such that they can afford to take larger risks. Again the classification of shares into preference and ordinary is calculated to appeal to investors of different degrees of conservatism. The preference shares, though not as safe as debentures, are considered safer than ordinary shares, which are subject to greater risks but which afford the possibility of very large returns.

The establishment of organised stock exchanges makes shares and debentures of companies easily marketable, thereby enabling investors to withdraw their investment in companies without difficulty. The ease with which an investor may get out of a company has an important bearing on his willingness to get in. An investor need not therefore be permanently wedded to a particular company.

Companies now universally embody the principle of limited liability, that is to say the liability of each shareholder is limited to the amount of shares held by him. It should, however be noted that the privilege of limited liability applies only to shares and not to debentures, as the debenture-holders are the creditors of the company.

The large accumulation of capital made possible by virtue of these privileges gives to the company unusual strength and stability, which in turn render its securities the more attractive to the investing public.

3. *Limited Liability.* The most important advantage associated with the system of joint stock enterprise is that of limited liability. In the modern world the typical joint stock company is a limited company, that is to say, it is registered on terms which carry the privilege of limited liability for its members. The debts of a partnership are the debts of each of its members to the full extent of his resources, all of which (not merely his share of the partnership property but his other property as well) may be seized for the payment of partnership debts. A limited company, however, stands between its own creditors and without the outside resources of its members. These creditors, having dealt with and trusted the company, must look to the company for payment. Since a company creditor does not recognise the individual members in the incurring of the debt, he cannot leap over the company in the process of collecting his debt and seize the personal property of the members of the company. All that belongs to the company the creditors can seize and sell. Its members may lose every rupee that they have

particular year may be considerably less than the amount distributed as dividend to shareholders; and the shareholders can claim a refund of tax in respect of such dividends to an amount in excess of the tax actually paid by the company for that year.

As the burden of taxation has been progressively increased during and after the last war, a large number of companies have been formed mainly for the purpose of enjoying the taxation concessions.

Disadvantages of Companies. We have seen above that joint stock companies enjoy certain statutory privileges such as corporate existence, corporate finance and limited liability, but in practice these facilities are sometimes abused. The following are the principal abuses that are associated with the system of joint stock enterprise;—

1. *Promotion Frauds.* The sale of securities of a joint stock company provides an almost ideal method for the victimisation of investors by those who are interested in the formation of the company, namely, promoters. In contrast to the ordinary commercial transactions where both parties bargain from comparatively equal positions, and where in case of necessity it is frequently open to the purchaser to verify the representations made as to the nature and value of what he is buying, the buyer of shares and debentures tends frequently to be at the mercy of the seller. He can know nothing or little about the real merits of the proposition except what the seller chooses to tell him. Impressed in many cases by the distinguished and high sounding names which appear on company prospectuses, he usually believes that all the necessary inquiries have already been made by the persons by whom these names are borne. But all is not gold that glitters. In regard to speculative shares the investor's hope and cupidity are often excited by the vision of high profits held out in the prospectuses. Even if all or most of the material facts are accurately set out in the prospectus, as they now have to be under statutory requirements, he may nevertheless through inexperience be unable accurately to gauge their true significance. And so long as the provisions of law are technically complied with, the window-dressing of the prospectus may be as artistic as the promoters want it to make, in which case an average investor is sure to be misled.

Abuses in the sale of securities may take several forms. The intention of the promoters from the very beginning may be fraudulent. More frequently, however, is the case where, though the object of the venture is really genuine, so intrinsically unsound proposition is presented to the public as being intrinsically sound. More subtle, but not less dangerous is that class of flotation where concerns are reconstituted and recapitalised on the basis of their present abnormal profits to the detriment of an indiscriminating investing public. In all such cases, the only interest of plausible but unscrupulous promoters and financiers is to make a quick profit on account of the readiness of the public to invest, but who themselves will be unscathed if the venture fails. Thus the public, during a boom period like the present, may pay a cash price so incommensurate with the

real value of the business that they may never receive an adequate return on their invested capital.

Moreover, the preliminary expenses, particularly by way of underwriting, in which the vendors and the promoters directly or indirectly participate, may be so swollen as seriously to impair the necessary working capital of the company.

On the subject of promotion frauds Mr. Sidney Webb, a well-known Socialist, wrote as follows in his foreword to a book entitled "*The Financiers and the Nation*":—

"We cannot be too plainly reminded of the way in which the public is periodically fleeced by financial tricksters and swindlers, because those highlights of capitalist enterprise are after each exposure quickly forgotten. It is remarkable how regularly during the past 100 years the story is repeated. Each decade sees a new variant, but the process is essentially the same. Tens of thousands of small investors, and also some large ones, are persuaded by lies and misrepresentations to purchase shares in what is simply a swindle. Hundreds of thousands, if not millions, of pounds are pocketed by the swindlers and the crowd of accomplices and parasites who in the ordinary course of business cooperate in what must not yet be termed as fraud. Presently there is a collapse, and more or less exposure; occasionally one or two of the chief swindlers get prosecuted and sentenced to prolonged imprisonment at the public cost. But there is no effective or prolonged publicity. All the influences in the City (i. e., London) combine to hush things up. Any angry talk is bad for business on the stock exchange. The banks fear the spread of panic and conceal their own losses. The newspapers are warned on behalf of influential people that any financial scandal interferes with legitimate business, and specially with the advertising of the 'promoters' and so the interest of the public in the latest financial swindle dies down. The figure of losses is concealed. Presently the crowd of small investors are ready to be robbed again, in some new guise.

"Meanwhile, it should be noted, hundreds of new swindles are carried on to the detriment of the public, without any overt criticism or public denunciation. How large is the proportion of rubbish among widely advertised articles, sometimes capitalised at a monstrous price extracted from the investing public, from patent medicines to cheap glow lamps, no one has ventured to compute. I do not remember that any professional economist has taken the trouble to estimate the total 'exchange value' during any one year of the various kinds of 'filth' that masquerade as 'wealth'.

2. *Irresponsible Management.* Although, as a matter of abstract theory, a joint stock company is a democracy, yet it tends more and more to become in practice an oligarchy of directors and managing agents, specially in this country. This concentration of control in the hands of a few people is brought about in several ways. In the first place, a company may issue securities of different types with differential voting rights attached to them. The management

acquire just those securities which carry the largest votes. In this way by contributing only a small fraction of the total capital of the company, control is secured over the majority of votes. Suppose a company raises a capital of Rs. 10,00,000 by issuing 5,000 preference shares of Rs. 100 each not entitled to any voting right, 45,000 ordinary shares of Rs. 10 each carrying one vote, and 50,000 deferred shares of Rs. 1 each also carrying one vote; and suppose that all the preference and ordinary shares are held by the public, while all the deferred shares are in the hands of the management. Then the management, just by contributing the precious sum of Rs. 50,000 command 50,000 votes as against 45,000 votes possessed by all the shareholders who have invested Rs. 9,50,000 in the company. This juggling with the votes attached to the different classes of shares is the simplest method of securing control.

Secondly, the vast majority of those who invest their money in joint stock companies have neither time nor ability nor inclination to regard these concerns in any other light than as mere agencies for the receipt of dividends. Shareholders, entitled to attend company meetings and by their votes to appoint directors to administer the businesses, cease in most cases even to consider the possibility of attendance or to regard themselves as in any way responsible for the conduct of the enterprises which are legally their property. This is natural and inevitable, for what collective influence can possibly be exercised by a constantly changing body of shareholders, scattered far and wide, unknown one to another and for the most part utterly ignorant of the conditions of the industry or the business in which their money is embarked? This apathy on the part of shareholders tends to concentrate control in the hands of the executives of companies.

Thirdly, in order to secure safe majorities for themselves, the directors and managing agents of companies possess other powers and resources such as the right to refuse transfers of even fully-paid shares and the extensive use of the proxy system. Those persons, who may be qualified and willing to take an intelligent interest in the affairs of companies, are sometimes kept back by the directors' power to refuse to register transfers of shares in the names of those whom they do not approve.

When a company becomes an oligarchy of directors and managing agents, they no longer remain responsible to the proprietors, because the latter are thereby rendered absolutely impotent in the matter of exercising any supervision over the company's affairs. The management may do what they like with the company. They may naturally use it for their private and personal ends and not for the benefit of shareholders.

3. *Exploitation.* Exploitation of companies by directors and managing agents is another serious abuse quite common in this country. The joint stock form of business organisation favours exploitation, because it separates ownership from control. There always has been, and will doubtless continue to be, exploitation by the powerful and influential of the needs of those who are

helpless. The company system has opened up now and previously unthought of fields and methods of exploitation. It requires a man of really strong character and of unusual conscientiousness to avoid the temptation of using an important office in a company for the sole purpose of building up his personal bank account. To the credit of company directors and managing agents, it must, however, be said that the great majority devote their undivided efforts to the service of the company and the shareholders whose interests they represent.

The various methods by which companies are exploited by their managing agents will be discussed in a subsequent chapter dealing with managing agents.

4. *Evils of Big Business.* The evils associated with big business will be discussed later on, but it must be noted that large scale enterprise has been built up on the company form of organisation. If there had been no company system, there would not have been in existence the gigantic business of today.

5. *Stock Exchange Speculation.* The organisation of business on joint stock principles has brought with it the evil of wild speculation which is a common phenomenon of all the stock markets of the world. In India the Bombay Stock Exchange is the hot-bed of wild speculation. Stock exchange speculation is facilitated by the easy transferability of company securities. The subject of speculation is described in detail in the chapter on 'Stock Exchanges.'

6. *One man Companies.* The provisions of company law are sometimes made use of in such a way as in effect to enable even a single individual to trade with limited liability. The process is simple. The owner of a business gets six other persons, mere dummies and nominees of his own, to join him. These seven persons subscribe the memorandum of association for one share each, often of nominal amount and register themselves as a company with limited liability. The company thus formed purchases the business from the owner and pays him for it in fully paid shares. No further shares are issued and no other members are admitted. The former owner of the business thus holds the entire share capital of the company except the six shares held by his six nominees, and retains complete control over the business, and in future he trades with limited liability. The process becomes still easier if it is desired to form only a private company where the minimum requisite is just two members.

In many cases this plan is adopted in perfectly good faith by the owners of large and valuable businesses, but the power of forming a limited company in this manner is obviously capable of abuse, and on occasions is most grossly abused. It is contended that such a proceeding was never contemplated by the legislature, but its legality has been established by judicial decisions. There is no doubt that a great many of the one-man companies are an abuse of the company law, and are formed merely for the purpose of obtaining the benefit of limited liability, so that if the business fails the creditors have recourse only against the company, and the proprietor escapes without any charge upon his private resources.

Company Contrasted with Firm. It may be useful to set out the main differences between a company limited by shares and a partnership. These are as follows :—

(a) A company is a legal entity in itself, distinct from the members who hold shares in it. It is governed by the Indian Companies Act of 1913 which it cannot override. Its powers are fixed by its memorandum of association. There is no limit to the number of shareholders except in private companies. The partners in a firm are individuals acting together in partnership as they may mutually agree amongst themselves, or in the absence of agreement, in accordance with the Indian Partnership Act. A firm is not a separate entity; it is the same as its partners. The members of a partnership may not exceed twenty in number, and if the business carried on is banking they may not exceed ten.

(b) The liability of a shareholder is limited to the amount which he has agreed to subscribe to the capital of the company, and when he has paid that amount to the company, no further liability attaches to him. The liability of a partner is co-extensive with the whole of his property. Every partner in a firm is jointly and severally liable with his co-partners for all the debts and obligations of the firm incurred while he is a partner.

(c) A shareholder has no power to bind the company or to bind his co-shareholders; nor has he any right to take part in the management of the company or to inspect its books except as may be allowed by the articles. The conduct of a company's business vests in the directors. A partner can bind the firm and his co-partners so long as he acts within the ordinary scope of the business. He is an agent of the firm and his co-partners for the purposes of the partnership. All partners can take part in the management of the business of the firm and all have access to its books.

(d) A shareholder can transfer his shares as he likes, subject to the articles, which in the case of a private company must restrict transfers. No matter what changes may occur in the personnel of the shareholders of a company, the company remains the same entity. A partner cannot, except by agreement with his co-partners, substitute another partner for himself. The death, insolvency or retirement of a partner, (where these events do not according to the agreement result in the dissolution of the firm) or the bringing in of a new partner, has the effect of creating a new firm.

(e) A company is bound by its memorandum and articles of association, and these documents can be altered only to a limited extent as provided by law. The partners can make any agreement they like and can vary the terms of the partnership when and as they please.

(f) A company must keep proper books of account and must prepare a balance sheet and profit and loss account every year. There is no statutory provision requiring a partnership to keep books of account and prepare a periodical balance sheet and profit and loss account, although it is practically essential.

(g) A company's existence can be brought to an end only by being

dissolved by order of the Court, or by being wound up in a legal manner, or by its name being struck off the Register where it has ceased to function. A partnership can be brought to an end by agreement at any time.

Co-operation

The three forms of business organisation (sole trader, partnership and joint stock company) discussed in the preceding pages are parts of the system of capitalism. We shall now consider another form of business organisation, namely, cooperation.

Cooperation is a form of organisation in which persons voluntarily associate together on a basis of equality for the promotion of their economic interests. Those who come together have a common economic aim which they cannot achieve by individual isolated action because of the weakness of the economic position of a large majority of them. This element of individual weakness is overcome by the pooling of their resources, by making self-help effective through mutual aid, and by strengthening the bonds of moral solidarity between them.

Cooperation is a form of economic democracy inasmuch as the constitution of a cooperative society is based on the equality of vote of each member. 'One man one vote' is the ruling principle, no member having more votes on the strength of his stake in the institution. The membership of a cooperative organisation is open, without restriction, to all persons who can derive a benefit from it. Further, the democratic outlook is reflected in the principle governing distribution of profits. Capital gets only a regulated moderate dividend, the surplus being distributed among members in proportion to their dealings with the undertaking. Rendering the best service to the members and not earning the highest profit is the aim set before a cooperative organisation. Cooperation has for its object the suppression of the evils of modern capitalism which may be summarised as follows :—

(a) The quantity of goods produced is ill-adjusted to the consumers' needs. At one time it is excessive through misjudgment and there is a glut in the market; at another it is deficient through a like error or through selfish action on the part of manufacturers and speculators, who may fill their pockets while the world suffers. At all times the consumer tends to pay an excessive price and the prime producer to receive an inadequate return, because each article passes through the hands of superfluous middlemen.

(b) The quality of goods is debased, because the producer is either dishonest or hard pressed by rivals. The consumer also, if he lacks credit, aggravates the trouble by buying the cheapest article without regard to its real value.

(c) Both producer and consumer are discontented, the latter through paying a high price for faked goods and the former because he is not master of his work and believes that he does not receive a fair return.

The cooperative movement encourages and teaches the citizen to do things for himself on the principle of mutual aid, and secures desirable results while avoiding the tendency to drab uniformity, regimentation and bureaucratisation.

As distinguished from other forms of social organisation, a cooperative philosophy of society must rest on free, universal association, democratically governed, conditioned by equity and personal liberty. It endeavours to strengthen the economic independence of its members by the development of agriculture, the promotion of organised methods of marketing, the improvement of industrial processes and by various other activities; it also aims at the promotion of all possible improvements whether in social customs, education or sanitation, and at the removal of all disabilities which hamper the growth of a rising standard of living. Its main purpose is the promotion of all-round well-being, increased production and better distribution being only the means towards the achievement of that end. It is a moral movement, the cooperative spirit helping to make better men and a better society.

History of Cooperation in India. The cooperative movement in India has passed through many vicissitudes. Four main stages in its history may be distinguished;—

(a) The cooperative movement in India may be said to begin with the passing of the Cooperative Credit Societies Act of 1904. The Act provided only for the formation of credit societies. Special stress was laid on rural rather than urban credit in view of the greater importance of the former in India, credit societies being distinguished as rural or urban according as at least four-fifths of their members were agriculturists or not. Unlimited liability was the rule in rural societies; in the urban societies the question was left to their option. Societies were subject to audit and inspection by officers deputed by Government and were exempted from payment of income-tax, stamp duties and registration fees.

There was a rapid growth in the number and activities of the societies between 1906 and 1911, and the Act of 1904 was found insufficient to meet the growing needs of the movement. In the first place it did not give legal protection to societies formed for purposes other than credit. Secondly the growth in the number of societies and the difficulty experienced in raising capital locally gave rise to the question of establishing some form of central organisation to provide capital to local societies and also to supervise them. These defects were removed by the Act of 1912, which granted legal recognition to productive and distributive societies and to different forms of central organisations. The distinction between rural and urban societies was abolished and in its place was substituted the classification of unlimited and limited liability societies. The immediate effect of the new Act was to give a fresh impetus to the growth of the movement. The number of societies, their membership and the amount of working capital increased steadily. New types of societies for the sale of produce, purchase of manure, and the retailing of farm implements and common necessities, were registered. Before fostering and supporting further growth, the Government wanted to be sure that the movement was developing on sound lines and appointed the Mackagan Committee in October 1914 to review the movement. The

Report of the MacLagan Committee made far-reaching proposals for the future development of the movement.

(b) Under the Reforms Act of 1919, Cooperation became a provincial transferred subject and was placed under the charge of a Minister. During the early years of the working of the reformed constitution, several provinces made progress on lines most suitable to their special requirements, Bombay giving a lead to other provinces by passing a *separate Cooperative Societies Act* in 1925. Non-official institutions for propaganda and education were encouraged. The expansion of the movement was rapid till 1929 when the depression set in and the various defects, which had been noticed by the MacLagan Committee but were partly obscured during the period of rising prices and prosperity, became prominent.

(c) The movement received a setback with the slump in agricultural prices and the consequent decline in the income of the farmer during the depression which began in 1929. A number of Committees of Inquiry were appointed in different provinces and states to suggest ways and means of reconstructing the movement, and consolidation, rectification and rehabilitation of the movement rather than expansion, leading to an increase in official control, were the predominant features of this period.

(d) The rise in agricultural prices that took place during and after World War II eased a difficult situation for the movement. There was a general tendency on the part of the agriculturists and members of cooperative societies to repay their debts both to the moneylenders and cooperative societies.

As a result of the war and the consequent introduction of economic controls and food rationing, a stimulus was imparted to the growth of consumers' cooperative stores, which were established to obtain food-stuffs at fair prices, and to cooperative marketing.

This last period is also distinguished by a new spirit of planning. Almost all the plans that have been proposed in recent times give an important place to the cooperative movement as a suitable agency for carrying out a number of their recommendations.

Formation and Management. A society may be registered with limited or unlimited liability. The conditions of registration are:—(i) Not less than ten persons can form a society, (ii) They must be above the age of 18 years, (iii) They must either reside in the same town or village or group of villages or must belong to the same tribe, class, caste or occupation; and (iv) They must file with the Registrar of Cooperative Societies a copy of the by-laws and other prescribed particulars.

The management of a cooperative society is democratic. It is in the hands of the members themselves, who appoint from their own body a committee to do the work for one year. The members of the managing committee receive no remuneration for their services. No member has usually more than one

vote; but where the liability is limited, a member may have more than one vote if prescribed by the by-laws. The accounts of every society are audited by or by order of the Registrar, who at all times has access to all the books, accounts, papers, etc.

The main privileges of cooperative societies are as follows :—(i) They are bodies corporate, that is to say, they have perpetual succession, common seal, legal right to make contracts, etc.; (ii) A registered society is entitled to priority to other creditors to enforce any outstanding debt due to the society from a member or a past member; (iii) The shares held in the society are not liable to attachment; (iv) On the death of a member his share is transferred to his heir, and (v) The societies are exempted from the payment of income-tax, stamp duty, and registration fees.

Distinction between a Cooperative Society and a Company. The following are the points of distinction between these two forms of business organisation :—

1. A cooperative society is governed by the Cooperative Societies Act while a joint stock company is subject to the Companies Act. Not less than ten persons can form a cooperative society, but for the registration of a public company there should be not less than seven persons. In the case of a private company only two persons are sufficient.

2. In a cooperative society the share list is always open to new members and the shares are never sold above their par value. The extent of a member's shareholding is limited to Rs. 1,000 by the Indian Act and Rs. 3,000 by the Bombay Act.

3. In a cooperative society the profits are distributed in proportion to his output of work or of business, the dividend taking the shape of deferred payment of savings. But in a joint stock company the profits are distributed in proportion to each member's capital holding. Thus a cooperative society is a union of persons and a company a union of capital; the former no doubt uses capital but it pays on it a fixed rate of interest.

4. In a cooperative society men own capital; in a company capital owns men. Hence a company is known as the capitalistic system. In a cooperative society the government is equalised among all the members, each having only one vote irrespective of his capital holding; but the government of a company is based on the extent of the holding of the share capital.

5. A cooperative society is not merely a business, but a combination of business and a spirit of service, which evokes loyalty, fellowship and a corporate feeling. It therefore appeals to self-interest as well as to social instinct. A company, on the other hand, is purely a business concern.

Different Forms of Cooperation

The principal forms of cooperative societies are credit societies, producers' societies, consumers' societies and miscellaneous.

(a) Credit Societies

The cooperative credit society is an association of persons of small or moderate means who from time to time need money for necessary or productive purposes and who in isolation cannot obtain it on reasonable terms. They may or may not contribute small shares to a common fund or capital. Broadly speaking in most countries agriculturists do not and non-agriculturists do make such contributions on an appreciable scale.

The prime object of their association is jointly to obtain credit, i. e., to be able to borrow as a society, and then to give credit to one another in the use of the money borrowed. The type of credit society now found in every civilised country is based on principles enunciated by Raiffeisen and Schulze-Delitzsch in Germany in the middle of the 19th century. The agricultural society follows Raiffeisen more closely, and the urban classes find the Schulze system more congenial.

The capitalistic evils of waste, adulteration and discontent take in the sphere of credit the forms of usury, extravagance and despair. The credit society meets and overcomes them by providing loans at a fair rate of interest, loans for useful purposes, and an equal status for each member, so that he may share in the government of his society, electing the officers and being himself eligible for election. All members alike support any loss that may arise through misfortune or dishonesty; all share in the increase of security and the lowering of interest which is derived from the accumulation of a reserve and the growing sense of unity among the associates.

Several kinds of cooperative concerns are found in India for the purpose of supplying credit, and these are :

(a) Rural Primary Credit Society (or Village Bank). The rural credit society is based on the Raiffeisen model, the most common form of primary society in India. The main features which according to cooperative theory such a society should possess are :—

1. A restricted area of operations to ensure mutual knowledge and mutual supervision.
2. Joint and unlimited liability (with safeguards) to enforce mutual control and vigilance and reassure the creditors. This is not, however an invariable feature, since in a few provinces some societies are being organised on the basis of limited liability.
3. Equal status of members and democratic control.
4. Honorary service on the executive to secure economy and promote self-help.
5. Allocation of profits to indivisible reserves, which are the principal bulwark of unlimited liability and make for financial stability and strength.
6. Limitation of loans to members only to safeguard the cooperative character of the movement, coupled with a careful selection of members on the basis of character.

7. Finally reliance on personal rather than material security.

Besides these, by now well-known primary principles necessary for the successful working of cooperative societies, there are certain canons of cooperative finance such as careful scrutiny of the objects of loans ; restriction of loans generally to productive purposes and the reduction of unproductive expenditure to the minimum ; careful supervision over the use of loans through a system of sureties over and above the general security of all society members and recall of loans in case of misuse ; insistence on the inculcation of thrift and attraction of local deposits, etc. Over and above all these comes the careful education and teaching of members and officials of societies in these principles.

(b) **Urban Primary Credit Society.** In the towns the credit society is commonly of the Schulze-Defitzsch type, based on limited liability and forming its capital largely by means of shares. Owing to the less concentrated intimacy of town life the moral element of mutual control is less marked, and, though accountancy and business procedure are on a higher level, the sense of unity and of common need are less developed than in a village.

Urban credit societies are the most important feature of the urban cooperative movement in India, and make up to some extent for the absence of joint-stock banking facilities in the smaller towns. The constitution of urban societies differs from that of rural societies. The area of operations is comparatively wide and the liability of members more usually limited. The capital is raised by means of shares and the societies accept deposits from members as well as non-members. They borrow at times from the central bank or the provincial cooperative bank, if one exists, when their own resources fall short of their requirements.

They advance loans mostly to the small traders, artisans, and salary earners on personal security as well as against gold, silver and produce. They accept deposits of various types and thereby afford facilities for investment to persons of small means.

Urban banking is especially well developed in Bombay and Madras where almost all the important towns are served by such banks. In Bombay their activities are co-ordinated by the Cooperative Banks' Association, which has rendered valuable service to the cause of urban banking.

(c) **District and Central Cooperative Banks.** These have in nearly all cases been founded by groups of public-spirited and comparatively wealthy men who contributed share capital and business ability in order to raise funds for the benefit of primary credit societies.

The central banks have been organised since the passing of the Cooperative Societies Act of 1912 to finance the primary credit societies and to act as their balancing centres. Broadly speaking, there are two types of central banks : the first having a membership confined to societies and known as banking unions, and the second having a mixed membership of individuals as well as societies.

The area of operations of central banks varies widely from a taluka or taluk in some provinces to a district or several talukas or taluks in other

provinces. Besides financing the affiliated societies, most central banks do other banking business such as the accepting of deposits, collecting bills, cheques, hundis, etc., issuing drafts and hundis, safe custody of valuables; and so on.

(d) **Provincial Co-operative Banks.** As the number and business of co-operative credit societies extended, and central banks multiplied, the need for a provincial bank to coordinate their functioning in the whole province became apparent. The Macleagan Committee strongly recommended the setting up of an apex bank in each of the major provinces, and such banks came to be established accordingly.

Though at the beginning of the movement the provincial co-operative banks used to finance village societies directly, they have now assumed the role of apex banks in almost all the provinces and do not generally have direct dealings with the societies except in the case of special types of societies, such as housing societies, etc.

The constitution of the provincial co-operative banks varies in different provinces. In some provinces the membership is open to individuals as well as to societies, and the board of directors consists of representatives of different types of societies as well as of individual members, while in others the membership is open to societies only and the board of directors consists exclusively of the representatives of the affiliated central banks, banking unions and other societies.

(h) Producers' Societies

The industrial population of Indian villages is decreasing owing to the keen competition between small crafts and rural industries on the one hand and large-scale industries on the other, and therefore an increasing number is seeking livelihood from land. The pressure on land is consequently increasing. The seasonal character of agricultural industry and the small size of his farm keep a villager who owns land idle for about 150 days in the year. The plight of a landless villager is very much worse—he has no independent occupation of his own, and his economic position is so weak that he cannot avoid sinking into a state of serfdom.

The two main problems which must be tackled before any substantial improvement in rural welfare can be expected are the relief of the pressure of population on the resources by measures calculated to improve per man hour productivity in general, and the transfer of a substantial proportion of the large mass of population from farming to non-farming pursuits. There must therefore be a deliberate policy for the occupational redistribution of the population now seeking its livelihood in one form or another from the overburdened land.

One of the most important avenues of employment for the surplus population is small-scale and cottage industries. The trend of well informed Indian opinion has always been in their favour, and it has also been suggested that for persons engaged in them the co-operative method of business is most suited. The Indian Industrial Commission (1916-18) stressed the intimate connection between

cooperation and cottage industries, and stated that industrial cooperative societies should be organised and assisted by the State in technical matters. The Royal Commission on Agriculture repeated the suggestion for organising village artisans on a cooperative basis for credit, raw materials and marketing. It is difficult to define the considerations on which the choice between large and small scale industries and cottage industries should be determined. The factors involved in the choice are numerous and often conflicting. But generally speaking, it may be stated that while in basic industries there is little scope for small industrial units, they have an important and useful place in consumption goods industries where their function is in many cases complementary to that of large units.

There are valuable lessons to be learnt in connection with industrial cooperatives from foreign countries. In pre-war Germany, one-eighth of the population subsisted on cottage industries, the small producers being grouped into associations which bought raw material for them in common and sold their finished goods. In Japan 60.70 per cent. of the industrial workers are employed in domestic industries, and more than 50 per cent. of the exports, measured in terms of value, are produced in these domestic factories. There are 20,000 handicraft cooperatives in Russia with a membership of 17,65,000. In the U. S. A. the idea of industrial cooperation is finding increasing acceptance. In China striking success in industrial cooperation has been achieved within a comparatively short period of time, although the success there is very largely due to the extreme scarcity of consumers' goods caused by the war.

Men of small means enter a cooperative society of production. By uniting their efforts and their contributions, they are able to collect a common fund, establish a common workshop, and if the nature of their profession permits, they undertake a joint contract of work. Usually a productive society unites with its prime function the duties of supply whether of professional or domestic requirements, or of sale of the goods produced, or both these duties together. Handloom weavers, who form an industrial cooperative society, may purchase their yarn in common, and weave and sell independently, or they may sell at a common shop the cloth which each has produced.

The object of producers' cooperative societies is to secure the advantages of (i) wholesale purchase of raw materials, (ii) an expert to supervise their methods of production and check the quality of their products, and (iii) an expert salesman who knows the market. The members of such societies evade the dangers of misjudgment resulting in waste and of bad quality.

The profit made by a producers' cooperative society, if distributed, will be proportional to the amount of goods which each member has sold to or through the society.

(c) Consumers' Societies

These will be considered in a subsequent chapter.

(d) Miscellaneous Societies

Cooperation is primarily a method which has been found peculiarly well adapted to the solution of certain problems and the removal of certain

evils. Organisation for credit is aimed at the avoidance of waste; cooperative production is a specific for labour unrest; and joint purchase has in view the substitution of good for adulterated commodities. In addition to these three main routes, there are many minor paths which the cooperator seeks to evade the onerous and rise to higher ground. A few of these may be mentioned briefly.

1. *Cooperative Insurance.* Insurance has been recognised all over the world as a scientific method of safeguarding and providing against the various hazards of life. Its growth has been encouraged in most countries by tax exemption and several other ways. It has, however, not made much headway in India principally for the reason that the bulk of the people live on the bare margin of subsistence and do not have any surplus to pay insurance premiums.

In several countries of Europe, the development of cooperative life insurance has been of considerable help in catering for the needs of agriculturists, artisans and workmen. In India life insurance on cooperative lines has made some progress during recent years in Bombay, Madras, Hyderabad and Baroda. Although the income of agriculturists is at present so low that there is no margin for any provision for the future, such a margin will, it is hoped, be created when the various development plans are implemented, and there will then be a scope for insurance. Something can, however, be done even now. There are in every village some agriculturists who are not in debt. These agriculturists who are on the margin of safety should be persuaded to take out insurance policies particularly marriage endowments and whole life limited payments. In times of prosperity some agriculturists have a surplus income which they spend on objects which are wasteful, or invest in gold or silver ornaments. In the years of adversity, on the other hand, debts are incurred on the pledge of ornaments which are generally lost as they become irredeemable on debts becoming too heavy. If an agency is created which will persuade the rural population to invest the windfall of good years in insuring against the adversity of bad years, it will perform a most useful service and remedy to some extent the evil of chronic and what seems to be inescapable indebtedness. The policy of insurance thus taken out will not only safeguard the future, but will also enable the policyholder to borrow in case of need at a fairly low rate of interest from the insurance society or better still from the village society on its security. The primary village societies and other cooperative organisations working in rural areas can render very great help in explaining the benefits of insurance and of the necessity of buying insurance policies instead of ornaments.

The cooperative insurance society will have, in certain respects, to adjust its methods of business to the special requirements of the rural areas. For instance, in cases of small policies of sums below Rs. 1,000, it will be worth its while to do away with medical examination and proof of age, and substitute for them a declaration from the proposer of good health and date of birth and a

confirmation of such a declaration by two other members of a cooperative organisation. In order to safeguard its interests, the society should lay down rules and conditions for the limitation of its risk during the first three years so that in the event of the death of a policyholder in the first year, his heirs will be entitled to receive only the amount of premium paid by him and in the event of his death in the second or third years, his heirs will be entitled to receive not the full sum assured but a proportion of it, say one-third and two-thirds. The society should accept full risk under the policy from the fourth year.

2. *Cooperative Housing.* Considerable interest has been aroused in recent years in the problem of town planning all over India, and a large number of cities and towns will have town planning schemes as part of the post-war development plans. On account of its various advantages, housing on a co-operative basis can well claim to be accorded a prominent place in these schemes of town planning.

In any housing scheme, cooperative effort has an advantage over private enterprise because it is primarily concerned with the interests of its members. It can ascertain the kind of houses the members want to build, and bring about cordial relations between its members as tenants and the members as landlords in their corporate capacity. It can give to its members freedom from the landlord's arbitrary interference and can arrange to share the responsibility and risk of ownership with its members.

Cooperative housing societies are generally of two main types : (i) tenants' cooperative societies, which build or purchase houses for sale or lease to their members, and (ii) building societies which facilitate the acquisition of houses through the grant of loans made on mortgage security.

Housing societies established on cooperative lines have been organised in certain provinces of India, but their activities have been confined to urban areas.

3. *Cooperative Transport.* With the development of roads on a large scale during the post-war period as planned by the Government of India and the provincial governments, numerous problems in connection with regulation of road and rail traffic and the maintenance of efficiency of the transport system will arise. These problems will be complicated by the fact that most of the motor transport vehicles are at present owned by an excessively large number of petty individuals who have insufficient resources and are ill-equipped to render efficient and cheap service to the public. In order to increase the efficiency of the transport system and to improve the economic conditions of the persons engaged in it, it is necessary to organise them on a cooperative basis. Moreover, transport organised on cooperative lines will be more amenable to State regulation than a host of individual lorry owners each plying his own vehicles.

4. *Multipurpose Societies.* It is generally accepted that our rural development schemes should be based on cooperative principles. Some type

of cooperative action is necessary. This may be taken either through single purpose societies or through multipurpose societies. A multipurpose cooperative society is one which renders a variety of service to its members.

As the supply of credit touches only one aspect of the life of the cultivator, the activities of the primary cooperative societies should be so extended as to cover the whole of his life. The primary credit society should therefore be reformed and reorganised so as to serve as a centre for the general economic development of its members. A multipurpose cooperative society may perform the following functions :—

- (a) To finance crop production ;
- (b) To act as an agent for the sale of produce to the nearest cooperative marketing organisation ,
- (c) To supply the farmer's simple needs for crop production such as seed, cattle feed, fertiliser and agricultural implements, and also consumer goods like cloth, kerosene, salt and matches ,
- (d) To serve as a milk collecting station for the nearest dairy and as a centre for animal first aid and maintenance of stud bulls ,
- (e) To serve as a centre for maintaining agricultural machinery for the joint use of the members , and
- (f) To encourage subsidiary occupations for its members.

The provincial governments are creating panchayats in rural areas ; therefore such functions as crop planning, irrigation, fuel plantation, management of pasture land and conservation of fodder may be left to be taken over by panchayats.

The arguments advanced against the multipurpose societies have been three : (i) It mixes up the accounts of the various activities and thus conceal the true position of any one type of activity , (ii) The failure in one respect may entail the winding up of other useful activities ; and (iii) Since the operations would become complicated, a few intelligent persons would come to control the society and this would be against the cooperative spirit. But these objections can be easily met. Separate accounts can be maintained for the various activities. The losses on account of any one activity are not likely to be so great as to necessitate the winding up of all activities of the society. The fear of the control of the society passing into the hands of a few arises because cooperative education has been neglected so far.

It is true that too many functions should not be tacked on to the objects of a multipurpose society. Credit societies should first be made to supply essential agricultural and domestic requirements and act as agents for the sale of the produce.

Test Questions

1. What are the advantages and disadvantages of a single entrepreneur business ? Discuss the prospects of such a form of business organisation in India.

(Agric. B. Com. 1948)

2. A solo trader whose business is expanding feels the need of some assistance in his business. Should he take a partner or engage a servant? Give reasons. *(Bombay B. Com. 1946)*

3. What are the requisites of an ideal partnership? Under what circumstances can a partnership be dissolved? *(Agra B. Com. 1948)*

4. What is partnership, and how does it differ from a joint Hindu family firm? *(Agra B. Com. 1946)*

5. Specify with reasons the important clauses which should be included in a properly framed partnership agreement. *(Agra B. Com. 1942)*

6. What are the advantages of registration of firms? How may a firm be registered? What do you understand by the principle of 'Holding out' in a partnership concern? *(Alld. B. Com. 1938)*

7. What are the chief characteristics of a joint stock enterprise? How do you account for the slow progress of this form of business organisation in India? *(Agra B. Com. 1947)*

8. Why is the joint stock company so popular as a form of business organisation? *(Bombay B. Com. 1945)*

9. Discuss, with special reference to the following statement, the principal abuses to which the system of joint stock enterprise is open in this country :— 'The distribution of shares among the various categories is so arranged as to ensure a controlling voice in the management to an individual or a small group.' *(Agra B. Com. 1944)*

10. What advantages does a limited company enjoy over other forms of business organisation? *(Agra B. Com. 1948)*

11. Being invited to interest yourself financially in a business, suggest the points would influence you in making a decision. *(Bombay B. Com. 1936)*

12. Compare the business position of a cooperative society with that of a joint stock company. *(Bombay B. Com. 1947)*

13. Discuss the future of co-operation as a form of business organisation in India. *(Bombay B. Com. 1946)*

14. What suggestions would you make in regard to the form of organisation suitable for cottage industries in India? *(Agra B. Com. 1942)*

CHAPTER 3

COMPANY ORGANISATION (1)

As already stated, the law relating to companies is contained in the Indian Companies Act of 1913, and sections mentioned in this and the following two chapters refer to this Act.

Methods of Incorporation. A company may be incorporated in any of the following three ways :—

1. *By Royal Charter* This method of incorporation applied especially where the corporation wished to exercise some of the prerogatives of the Crown, such as the government of a territory, the raising of a military force or matters of that kind. The right to exercise these powers is given to the company by the terms of the charter. A well-known example of a company formed in this way is that of the East India Company. This method is rarely adopted nowadays.

Companies incorporated by royal charter are called chartered companies. Very often they use the word chartered as part of their name, e.g., the Chartered Bank of India, Australia and China. Where the liability of the members of a chartered company is limited, it is not usually necessary to use that word as part of the name.

2. *By Special Act of Legislature.* This method of incorporation is followed in the case of companies formed for the purpose of carrying on some business of national importance. Such companies are known as statutory companies. Each statutory company is governed by the terms of its special Act. There are a number of statutory companies in India, which have been formed either by special Act of the British Parliament or by special Acts of the Indian Legislature. Examples of such companies are the various sterling Railway Companies such as the East Indian Railway Co., the G. I. P. Railway Co., the Imperial Bank of India, the Reserve Bank of India, and the Industrial Finance Corporation. Like chartered companies, statutory companies are also limited companies, but they are not required to use the word limited as part of their names.

3. *By Incorporation under the Indian Companies Act.* This is the usual method of incorporation available to any company, the other two methods being rarely used. Barring a few chartered and statutory companies, all companies have been formed in this way.

Prohibition of Large Partnerships. Section 4 provides that not more than ten persons can combine together for carrying on a banking business, nor more than twenty persons for carrying on any other kind of business, unless the association is registered under the Indian Companies Act or is formed in any of the other two ways. An association of more than twenty persons, which exists not for gain but for some other purpose such as the promotion of art, charity,

etc., does not require registration. The object of the law is to prevent the mischief arising from large trading undertakings being carried on by large fluctuating bodies, so that persons dealing with them do not know with whom they are contracting and so may be put to great expense, which is a public mischief to be repressed.

The term persons includes any company or association or a body of individuals whether incorporated or not. Therefore a joint Hindu family as represented by its manager or karta counts as one person, because it is regarded in Hindu law as a distinct entity by itself irrespective of the varying number of members composing it. It is, therefore, expressly laid down that section 4 does not apply to a joint Hindu family carrying on the family trade or business. However, if two or more such families form a partnership, minors are to be excluded in computing the number of persons. If a joint Hindu family carries on its own business, section 4 does not apply to it, but if one or more joint Hindu families combine with one another for carrying on a business, each joint family shall not count as one person but as many persons as there are adult members in each of the joint families. A registered company would, of course count as one person.

An association formed in contravention to section 4 is an illegal association. An illegal association is a phantom, it has no legal existence. The consequences of an illegal association are as follows :—

1. An action by an illegal association, whether against a member or any other person, will fail if the illegality of the association is disclosed. Such an association cannot sue, even if it is subsequently registered.

2. Every member of an illegal association is personally liable for all liabilities incurred in the business. It means that a suit would lie against every member of an illegal association and not the association as such for enforcing all liabilities incurred in the business of such association, irrespective of whether the plaintiff had no notice of the illegality of the association.

3. Every member of an illegal association formed after 15th January 1937 is punishable with fine not exceeding Rs. 1,000.

Kinds of Companies. The Act provides for the registration of three distinct kinds of companies, viz.— companies limited by shares; companies limited by guarantee; and unlimited companies. The principal form of registration is that of a company limited by shares, whereby each person becoming a member of the company acquires one or more of the shares into which the capital is divided, his liability being limited to the amount for the time being unpaid on the shares held by him. A company limited by guarantee is a company having the liability of its members limited by the memorandum to such amount as the members may respectively thereby undertake to contribute to the assets of the company in the event of its being wound up. Such companies are either those having a share capital or those not having a share capital. An unlimited company is little more than an ordinary partnership, each shareholder being liable for the debts of the company to the last pice. He is, however, free from liability at the

end of a year from his ceasing to be a member. Such companies are practically non-existent.

Again, the companies that may be registered under the Act are divided into private and public companies. A private company is one which by its articles restricts the right to transfer its shares, limits the number of its members (exclusive of present employees) to fifty, and prohibits any invitation to the public to subscribe for any shares or debentures of the company. All companies that are not private companies are deemed to be public companies.

Companies limited by guarantee and unlimited companies are quite unsuitable for commercial undertakings. It is with the formation and administration of companies limited by shares that we are principally concerned.

Flotation of Public Limited Companies

There are two terms—company formation and company flotation—that are often used as having the same meaning. But strictly speaking there is an important difference between them. Flotation is a wider term than formation. Formation may be taken to mean the creation and bringing into being of the legal entity to voyage upon the sea of commerce. Flotation may be described as the launching of the craft, completed and equipped for its voyage of unknown duration. Thus the flotation of a company includes not only its formation, but also the raising of capital needed for its business and the completion of all those legal formalities which are necessary before it can validly commence business.

The Promoter. A certain amount of preliminary work is necessary before a company can be brought into existence, and the person who carries out this work is called the promoter, who may be an individual, firm or company. It is difficult to frame a good definition of the term promoter which is not a term of law but a term of business used to describe the person or persons who undertake to form a company with reference to a given object and to get it going, and who take the necessary steps to accomplish that purpose.

A limited company may be formed either to take over an already existing business by purchase or lease, or start an entirely new one, and the work of the promoter in this connection is as follows:

1. To conceive the idea of forming a company and to explore its possibilities.
2. To get together a number of persons who may sign the memorandum of association and act as its first directors.
3. To settle the name of the company, the amount and form of its capital and to arrange for underwriting, if necessary.
4. To select banks, auditors, brokers and legal advisers.
5. To have the memorandum and articles of association and the prospectus drafted.
6. To attend to the registration of the company.
7. To arrange for the completion of contracts with vendors, underwriters and managing agents.

8. To do the filing, issue and advertising of the prospectus.
9. To pay preliminary expenses.
10. To secure allotment of shares and debentures.
11. To take steps to obtain the certificate entitling the company to commence business.
12. To arrange for office, factory, machinery and the necessary staff.

In India there are no specialist agencies for doing the work of company promoters; and persons who want to become managing agents usually act as promoters. Such persons first act as pioneers, then as promoters and finally as managing agents. As the managing agents wield a powerful influence over the management of companies in this country, it has been very aptly remarked that they are *pioneers cum promoters cum managing agents cum overlords*—all rolled into one.

Preliminary Contracts. When a company is to be formed for the purpose of purchasing or leasing an existing business or some other property, the promoter naturally would not like to incur the expense of forming it until a binding contract has been made with the vendor or lessor. These contracts are made between the promoter on the one hand and the vendor or lessor on the other, and as such they are not and cannot be binding upon the company. Such contracts are usually made voidable by either party in the event of the proposed company not being formed, the minimum subscription not being obtained, or if the company is formed and does not adopt the contracts within a specified period. As the company is not a party to the contracts, it is usual for the company, when formed, to enter into new agreements in terms similar to those adopted in the original contracts, in order that the promoter may be relieved of liability.

Promoter's Remuneration. The promoter has frequently to do a lot of work in connection with the flotation of a company, and it is only fair that he should be remunerated for his services. He may be remunerated in any of the three ways:—He may pass on the business or other property to the company at inflated price; he may be given a commission on the purchase price of the business or property taken over by the company; or he may be granted a certain lump sum as remuneration. The promoter's remuneration may be paid in cash or partly in cash and partly in shares and debentures of the company. It will be pointed out later on that whatever remuneration the promoter gets is to be disclosed in the company's prospectus. It may however be stated that in India the promoters, in order to become the managing agents of the companies they promote, do not take any remuneration for their services, because as managing agents they will be able to earn a lot.

Formation of a Public Limited Company. The following steps are necessary in order to procure the registration of a new company:—

1. Filing the documents named below with the Registrar of Joint Stock Companies of the Province in which the registered office of the company is to be situated:—

(a) The Memorandum of Association and the Articles of Association signed by seven persons (Section 22). If a company adopts Table A in its entirety, it need not file any special articles, but the fact must be endorsed on the memorandum. The memorandum and articles require a stamp duty, which differs in the different provinces of India.

(b) A list of persons who have consented to become directors of the company (Sec. 84).

(c) Where the directors are appointed by the articles, each such director must sign and file with the registrar (a) a written consent to act as director, and (b) either sign the memorandum for a number of shares not less than his qualification (if any), or take from the company and pay or agree to pay for his qualification shares, or sign and file with the Registrar a contract in writing to take from the company and pay for his qualification shares (if any), or make and file with the Registrar an affidavit to the effect that a number of shares not less than his qualification (if any) are registered in his name (Sec. 81).

(d) A statutory declaration that the requirements of law for registration have been duly complied with (Sec. 21).

(e) Notice of the situation of the company's registered office (Sec. 72).

(f) Prospectus or Statement in lieu of prospectus (Secs. 92 and 98).

N. B.—Number (e) and (f) may be filed either at the time of registration or shortly afterwards.

II. Payment to the Registrar of the following fees. The fees may be paid by depositing the required amount into a Government treasury.

(a) Duty Payable by a company having share capital.

	Rs.
Where the capital does not exceed Rs. 20,000	10
Where the capital exceed Rs. 20,000 —	
For every Rs. 10,000 or part thereof up to Rs. 50,000	20
For every Rs. 10,000 or part thereof beyond Rs. 50,000 and up to Rs. 1,00,000	5
For Every Rs. 10,000 or part thereof beyond Rs. 1,00,000	1

The maximum duty payable is Rs. 1,000, and this maximum is reached when the capital is Rs. 52,50,000. Moreover, whenever the share capital of a company is increased, only such additional duty becomes payable as represents the difference between the duty that would have been required to be paid, if the increase had formed part of the original share capital and the duty that has actually been paid. If a company is originally registered with a share capital of Rs. 10,00,000, it pays Rs. 575 as duty thereon. If subsequently its share capital is increased to Rs. 15,00,000, the extra duty payable will be only Rs. 50, because the duty on Rs. 15,00,000 is Rs. 625, and Rs. 575 has already been paid at the time of the company's registration.

(b) Filing Fees.

For every document filed with the Registrar a filing fee of Rs. 3 has to be paid.

Certificate of Incorporation. After the filing of the necessary documents and the payment of the prescribed duty and fees, the Registrar, if he is satisfied that everything is in order, grants a certificate of incorporation stating that the company is incorporated and is limited. The effect of incorporation is that the subscribers to the memorandum, together with such other persons as may from time to time become members of the company, become a body corporate, with a distinct entity from such members and having a perpetual succession with a common seal and with the liability of the members limited to the amount for the time being unpaid on the shares held by them.

The three important documents, namely, the memorandum of association, the articles of association, and the prospectus will now be considered in detail.

(a) Memorandum of Association

This is the most important document, as it forms the charter of the company and is, so to say, the 'statutory deed of partnership.' It contains the fundamental conditions upon which alone the company is granted incorporation. It proscribes as well as limits the liability of the members. All acts exceeding the powers taken in the memorandum are *ultra-vires* the company, i.e., beyond its powers, and are therefore null and void. The memorandum of association of a company limited by shares must state—

- (a) The name of the company with "Limited" as the last word in its name;
- (b) The province in which the registered office of the company is to be situate;
- (c) The objects of the company;
- (d) That the liability of the members is limited;
- (e) The amount of shares capital with which the company proposes to be registered and the division thereof into shares of a fixed amount.

It concludes with a declaration of association wherein the subscribers to it state opposite to their names the number of shares they respectively agree to take. The signatories must sign in the presence of at least one witness who must attest the signatures.

Name of Company. Subject to the restrictions mentioned below any name may be chosen for the company. It is advisable for the promoter of a proposed company to ascertain from the Registrar whether the desired name is available for registration, because if the proposed name were not accepted much trouble and necessary expense would be caused. It is usual to select a name which gives some indication of the company's business. It is not necessary that the word 'company' should form part of the name. The name of a company may include personal names or it may be of an impersonal character. In the former case the valuable goodwill and reputation attached to a personal name is retained.

(a) The name should not be identical with that of another existing registered company or so nearly resembling that name as to be calculated to deceive, except where the company in existence is being dissolved and signifies

its consent in such manner as the Registrar may require (Section 11).

(b) The words Crown, Emperor, Empress, Federal, Imperial, King, Queen, Royal, State, Reserve Bank, Bank of Bengal, Bank of Madras, Bank of Bombay, or words expressing the sanction, approval or patronage of the Crown or the Government of India or a Provincial Government must not be used as part of the name, except with the previous sanction of the Central Government being obtained in writing (Section 11).

(c) Under the provisions of the Co-operative Societies Act, every company not registered under the Act is prohibited from using the word 'Co-operative' as part of its name without the sanction of the Provincial Government.

(d) The name should not contain the word Municipal or Chartered or any other word which suggests or is calculated to suggest connection with any municipality or other local authority or with any society or body incorporated by royal charter.

(e) In the case of a company limited by shares the word Limited or any recognised contraction thereof such as Ltd. must be used as the last word of the name.

Section 73 requires that a limited company's name must (a) be painted or affixed on the outside of every office or place where it transacts business in English as well as in one of the vernaculars used in that place; (b) be engraved in English on its seal, and (c) be mentioned in English in all notices, advertisements, and other official publications of the company, and on all hundis, bills of exchange, promotes, cheques, etc., and on all orders for money or goods and in all invoices, receipts, letters, etc.

The name of a company can be altered in two ways under section 11:—

- (i) If a company has inadvertently registered a name similar to that of an existing company, it can be changed simply with the sanction of the Registrar;
- (ii) In other cases, the name can be changed only by passing a special resolution and with the approval of the Provincial Government obtained in writing.

Registered office: The memorandum of association does not show that address of the registered office, but states only the province in which it sitsuate. Section 72 requires that a company shall as from the day on which it begins to carry on business or as from the twenty-eighth day after the date of incorporation, whichever is earlier, have a registered office to which all communications and notice may be addressed. Notice of the situation of the registered office and of any change therein shall be given within twenty-eight days after the date of the incorporation of the company or of the change, as the case may be, to the Registrar who shall record the same. The address of the registered office may be freely changed from one place to another in the same province; but if it is to be changed from one province to another, certain requirements of law must be complied with. These requirements are stated under the next heading.

Objects of the Company. The objects clause in the memorandum of association is of the highest importance, because it not only defines but also limits the scope of a company's operations. It is, therefore, essential that this clause should be framed with the utmost care. The objects of a company must not be illegal, that is to say, they must not include anything which is against the Indian Companies Act or against any other law. For example, power cannot be taken by a company to buy its own shares, to pay dividends out of capital, to restrict the auditors from disclosing certain facts to the shareholders, to prohibit the shareholders from filing a petition for winding up, or to do any act contrary to public policy.

The objects should be stated fully and clearly and should include everything which may be necessary to enable the company to carry on its business, as the powers of a company to transact business are limited to the objects specified in the memorandum. Everything beyond the scope of the memorandum is *ultra vires* the company, absolutely void and incapable of ratification even if all the shareholders assent to it. Therefore, in practice, this clause is made as wide as possible.

Persons dealing with a company are deemed to have notice of the provisions of the memorandum, and to have notice of the limitation of the company's powers therein contained; and if they do not ascertain the extent of such limitations they enter into dealings with the company at their own risk.

If a company wishes to alter its registered office from one province to another or to alter the objects clause of its memorandum, it can do so only by passing a special resolution confirmed by the Court, and then only if the change will enable it (a) to carry on its business economically or more efficiently; (b) to attain its main purpose by new or improved means; (c) to enlarge or change the local area of its operations; (d) to carry on some other business which may be conveniently combined with its own; (e) to restrict or abandon any of its objects; (f) to sell or dispose of the whole or any other company or body of persons (section 12).

Share Capital. The amount of capital with which the company proposes to be registered and the number of shares into which it is divided are to be stated in the memorandum. It is not necessary to distinguish the different classes of shares in this clause of the memorandum, as this can be done by the articles. If a distinction between shares of two or more classes is not made in the memorandum, it does not necessarily imply that all the shares are to be on equal footing, for in that case the articles may authorise the issue of shares carrying different rights. If the rights attached to the different classes of shares are defined in the memorandum, they cannot be altered except as provided for in section 153. The rights defined in the articles can, however, be altered simply by means of a special resolution of the company, so long as there is no special contract to the contrary between the company and the shareholders whose rights are proposed to be altered.

It is usual and prudent to word the capital clause so as to provide for powers to increase, reduce, convert, subdivide and consolidate the share capital and to issue any of the shares in the capital, original or increased, with or subject to any preferential, special or qualified rights or conditions as regards dividends, repayment of capital, voting or otherwise, and to vest in the directors, by making a provision in the articles, the power to issue shares with any preferential, special or qualified rights as aforesaid. By so doing, the directors are in a position to control the character of shares required to be issued according to the changing exigencies and requirements of the company, without necessitating any amendment of the memorandum and the articles either.

If so authorised by its articles, a company may (a) increase its capital; (b) consolidate and divide all or any of its share capital into shares of larger amount; (c) convert its paid up shares into stock and reconvert that stock into paid up shares of any denomination; (d) subdivide its shares or any of them into shares of smaller amount, and (e) cancel shares that have not been taken up or agreed to be taken up, and to diminish its capital by the amount of the cancelled shares (section 50). The powers conferred by this section must be exercised by the company in general meeting. Usually a company takes power in its articles to do all these things.

If so authorised by its articles, a company may by special resolution after confirmation by the Court reduce its share capital (a) by extinguishing or reducing the liability on any of its shares in respect of share capital not paid up; (b) by cancelling paid up share capital which is lost; (c) by paying off any paid up share capital which is in excess of the company's wants, (d) in any other way (section 55). A special resolution under this section is called a resolution for reducing share capital.

If the memorandum or articles contain provisions for varying the rights of any class of shareholders subject to the consent of any specified proportion of the holders of the issued shares of that class, and at any time the rights are so varied the dissenting shareholders have, under section 66A, a right to apply to the Court for the cancellation of such variation.

Under section 163 it is possible to put through any scheme of arrangement between the company and its members. The scheme may involve a reorganisation of the company's share capital.

A Company may, under section 69, determine by special resolution that any specified portion of its share capital not called up shall not be capable of being called up except in the event and for the purpose of the company being wound up. Such a portion of the share capital is known as *reserve capital*.

Limited liability. The memorandum of association states that the liability of the members is limited. It is not possible to make the limited liability of the members of a limited company unlimited, but the memorandum may provide under section 70 for the unlimited liability of the directors. And if the memorandum does not so provide, it can be altered (if so authorised by the

articles) by passing a special resolution so as to render the liability of its directors unlimited.

(b) ARTICLES OF ASSOCIATION

The articles of association of a company are the regulations or bye-laws for carrying into effect the objects defined in its memorandum of association and for the management of its internal affairs. The 'articles' means the articles of association of a company as originally framed or as altered by special resolution. The articles are subordinate to the memorandum and they cannot go beyond the scope of the Act and the memorandum.

The articles must be printed, must be divided into paragraphs consecutively numbered, and must be signed by each subscriber of the memorandum.

Application of Table A. Table A is a model set of 116 articles printed in the First Schedule to the Act. A public limited company may adopt Table A wholly; or adopt it to the extent that it satisfies its requirements, framing special articles to meet special needs; or draw up and register its own special set of articles. If no special articles are filed, the memorandum must be endorsed "Registered without Articles" and in that case every member of the company is bound by Table A.

Private companies, unlimited companies and companies limited by guarantee must file their own articles, as they cannot adopt Table A in its entirety. The articles of a private company must include provisions in accordance with section 2 (13) and also bar certain clauses of Table A which are inapplicable to private companies. In the case of a company limited by guarantee or an unlimited company, under section 17 (3), the articles must state the amount of share capital, and, if it has no share capital, the number of members with which the company proposes to be registered in order to enable the Registrar to calculate the duty payable.

Section 18 provides that, in the case of a company limited by shares (whether public or private), if articles are not registered, or, if articles are registered in so far as the articles do not exclude or modify the regulations of Table A, those regulations shall, so far as applicable, be the regulations of the company in the same manner and to the same extent as if they were contained in duly registered articles. Moreover, under section 17 (2) regulations 56, 66, 71, 95, 97, 105, 107, and 112-116 of Table A compulsorily apply to all companies, and regulations 78-82 only to public companies.

Subject-matter of Articles. The articles of a company usually deal with following matters:—Exclusion or modifications of Table A; adoption of preliminary contracts; number and value of shares; allotment of shares; issue of share certificates; calls on shares; company's lien on shares; forfeiture or surrender of shares; transfer of shares; increase of capital; reduction of capital; borrowing powers of the company; rules regarding general meetings; appointment, remuneration, powers, etc., of directors and managing agents; declaration of dividends and transfers to reserves; keeping of books and audit; rules as to notices; payment of commission and brokers;

inspection of the books of the company; and such other matters as may be necessary for the administration of the company.

In accordance with the provisions of the Act a company can exercise certain powers only when it is authorised to do so by its articles, and if the articles do not confer the necessary authority, they must first be altered by means of a special resolution in order to take the necessary power. Such matters are given in sections 41, 43, 46, 49, 50, 55, 66, 71, 85, 91, 101, (7), 105, 103.B, 107, 108, and 125.

Effect of Articles. Under section 21 the articles bind the company and the members (as well as their heirs and legal representatives) to the same extent as if they had been signed by each member and contained covenants by each member to observe them. The articles constitute a contract between the company and its members in their capacity as members. Thus the company can bring an action against a member for his not observing the provisions of the articles, for example, non-payment of calls. Similarly a member, whose shares have been forfeited by the company against the provisions of its articles, may sue the company. The articles are not, however, binding upon the company in its relations with the outsiders or even its members where a right is claimed by such members not as members but in some other capacity. This is so because the outsiders are not a party to the articles of the company.

Upon registration, the memorandum and articles of a company become public documents and anyone who has dealings with a registered company must be taken to have notice of the memorandum and articles. Every joint stock company has its memorandum and articles of association open to all who are minded to have any dealings whatsoever with the company, and those who so deal with it must be affected with notice of all that is contained in those two documents. By this rule every one is deemed to have notice of the memorandum or articles and all outsiders are deemed to have notice not only of the company's powers but also of the directors' powers and the limitations imposed thereon. For example, if the articles provide that a bill of exchange to be effective must be signed by two directors, anyone who takes the same must see that it is so signed, for otherwise he cannot claim under it.

Alteration of Articles. Section 20 says that, subject to the provisions of the Act and to the conditions contained in its memorandum, a company may by special resolution alter or add to its articles and any alteration or addition so made shall be as valid as it originally contained in the articles and be subject in like manner to alteration by special resolution. The restrictions imposed on the powers of alteration of the articles of association as either statutory restrictions or restrictions imposed by the past judicial decisions.

Statutory Restrictions.

1. Alterations in the articles can be made only by a special resolution and not by an ordinary resolution, even though the articles lay down the latter procedure (Sec. 20).

2. The alteration must not go beyond the provisions contained in the memorandum of association (Sec. 20).

3. The alteration must not be such that it contravenes any of the provisions of the Indian Companies Act (Sec. 20).

4. The alteration must not be such that it imposes on any member the obligation of buying or subscribing for more shares or increases his liability or forces him to pay money to the company, provided the member has not agreed in writing to be bound by such alteration (Sec. 20A).

Restrictions Imposed by Judicial Decisions.

1. The power of alteration cannot be used to oppress or defraud a minority of shareholders, nor will the Court allow a majority to commit a fraud on the minority.

2. The alteration should not be such as to enable the company to commit a breach of contract with an outsider.

3. The power of alteration should be exercised bona fide for the benefit of the company as a whole.

Distinction between Memorandum and Articles. The following are the salient points of distinction between these two important documents which are the title deeds of a company :—

1. The memorandum contains the conditions upon which alone the company is granted incorporation—conditions which are fundamental and unalterable. The articles are the internal regulations of the company and over these the members have full control and they can be easily altered.

2. The memorandum cannot give the company power to do anything contrary to the provisions of the Act. The articles are not only limited by the Act but are also subsidiary to the memorandum and cannot exceed the powers contained therein.

3. The memorandum is in the nature of a contract between the company and the outside world dealing with it; therefore a person dealing with a company is supposed to know the provisions of its memorandum. The articles, however, do not create a contract between the company and outsiders. Though a person dealing with a company is supposed to know the provisions of its articles, yet if there is a breach of those provisions, he is not affected thereby, provided the matter was within the powers of the company as defined by its memorandum and he had no notice of the breach.

4. The memorandum contains the objects and powers of the company. The articles provide the regulations by which those objects and powers are to be carried into effect.

5. The memorandum cannot be altered except as regards certain specified particulars and in accordance with the provisions of the Act. The articles, being the internal regulations of the company, stand on a very different footing and are in the powers of the shareholders themselves, who can alter them by special resolution at any time.

Doctrine of Ultra Vires. The term '*ultra vires*' (beyond the power) denotes a very important legal principle that applies to all corporations. The principle is that a corporation is formed only for certain specified purposes, which are defined by its charter, and any act beyond the powers conferred is null and void and has no legal effect. In the application of this doctrine to limited companies there are three classes of *ultra vires* acts, viz :—

(a) Those that are *ultra vires* the memorandum, e. g., engaging in any business not covered by the object clause of the memorandum. Such acts are entirely void.

(b) Those that are *ultra vires* the articles but *infra vires* the memorandum, e. g., paying interest on calls in advance at a rate higher than that allowed by the articles. Such acts are also void, but the company in general meeting may alter the articles by a special resolution and ratify any such unauthorised acts. Whenever any such act is ratified, the provisions of the Indian Contract Act relating to the principles of ratification must be observed.

(c) Those that are *ultra vires* the directors but *infra vires* the company, e. g., payment of a gratuity to an employee of the company by the directors who are not authorised to do so. The company in general meeting may ratify this class of acts by passing an ordinary resolution. If the company desires to give the directors additional powers for the future which are not provided for by the articles, a special resolution is necessary, as this would involve an alteration of the articles.

(c) Prospectus

Definition. Section 2 (14) defines the prospectus as any prospectus, notice, circular, advertisement or other invitation, offering to the public for subscription or purchase any shares or debentures of a company, but it does not include any trade advertisement which shows on the face of it that a formal prospectus has been prepared and filed. Moreover, according to section 93 (3), a circular to existing members or debenture-holders of a company inviting them to buy further shares or debentures is not a prospectus, whether such circular is with or without the right to renounce in favour of other persons.

After the company has been registered and the certificate of incorporation obtained, the next thing for the promoters to do is to secure the capital required for trading purposes. In some cases this capital may be available privately, as the persons responsible for bringing the company into existence may be willing to provide all that is necessary at least for the time being. But usually an invitation is issued to the general public to subscribe the capital. Legally it is possible to issue a prospectus even before a company is formed; and a company may issue a prospectus at any stage in its existence and not merely at the commencement.

Filing. Section 92 requires that every prospectus must be dated, a copy must be signed by every director or proposed director and filed with the Registrar, and the prospectus must state on the face of it that a copy has been so filed.

Preparation. There appears to be no restriction as to the form in which a prospectus may be produced, provided that it conforms to the requirements of the law—not only the law as applicable to companies, but also to the law in general. It may be printed in book or pamphlet form, or in colours, or it may be accompanied by photographs and pictures.

Circulation. A prospectus may be circulated by post or otherwise, or it may be advertised in the press. In practice many companies adopt both methods of publicity. They advertise the prospectus in newspapers and also make its copies available to the public through banks and brokers.

Contents. The prospectus is the very foundation of a company's edifice. It is on the basis of the statements made in the prospectus that the public makes applications and offers for the shares or debentures of the company. Therefore the law is very stringent on the subject. One of the things necessary in order to protect the investing public is to provide them with all relevant information that will enable them to arrive at a decision as to whether they should or should not apply for shares or debentures of the company. The abuses which the law has intended to remedy are that material facts are often suppressed; the directors have frequently no stake at all in the company; many companies start business with hopelessly inadequate capital and consequently fail; much of the money subscribed is watered; and in many cases the managing agents are appointed with excessive remuneration and very wide powers.

The object of law governing company prospectuses is very aptly stated in the following words of a foreign Commission: "We are not so optimistic as to believe that any legislation, however wisely conceived and effectively administered, will prevent all foolish investments or all unsound company promotions. We have indeed no right, even if we had the desire, to take away from the citizen his inalienable right to make a fool of himself. We do, however, feel that we have the right to attempt to prevent others making fool of the citizen." In other words, if the law cannot prevent a fool from his folly, there is no reason why it should not give a prudent man guidance.

Section 93 lays down that every prospectus issued by an existing or a proposed company must contain the information summarised below. Any condition binding the applicants for shares or debentures to waive the provisions of this section is declared void by Section 96 (1); while section 96 (2) lays down that no application form must be issued by the company unless it is accompanied by a full prospectus complying with the law. This restriction, however, does not apply to underwriters or to shares not offered to the public.

(a) Prospectus issued by a new company

1. Objects.

*The contents of the memorandum of association of the company with the names, descriptions and addresses of the signatories and the number of shares subscribed for by them respectively. This information may, however, be omitted if the prospectus is published as a newspaper advertisement.

2. Directors.

*1. The names, descriptions and addresses of the directors. This should not be done unless the requirements of section 81 regarding the advertisement of directors have been complied with.

*2. The share qualification and remuneration of directors.

*3. The direct or indirect interest of every director in the promotion of or the property to be acquired by the company, and any sum paid to him to induce him to become or to qualify him as a director.

4. Any restrictions imposed by the articles on the directors' power of management.

5. The dates of and the parties to every contract regarding the appointment and remuneration of a managing director and the time and place at which it may be inspected.

3. Managing Agents.

*1. The names, descriptions and addresses of the managers and managing agents

2. Any provision in the articles or in any contract regarding the appointment and remuneration of managers and managing agents.

3. Any commission on shares and debentures and any discount on shares payable to managing agents.

4. The dates of and the parties to every contract regarding the appointment and remuneration of managing agents and the time and place at which it may be inspected.

4. Share Capital.

1. The number of founders or management or deferred shares (if any) and the nature and extent of the interest of the holders in the property and profits of the company.

2. The number of redeemable preference shares with particulars of redemption.

3. Where the shares are of more than one class, the rights of voting and the rights as to capital and dividend attached to the several classes of shares.

4. Restrictions imposed by the articles on the members' right to attend, speak or vote at general meetings or on their right of transfer shares.

5. The amount payable on application and allotment on each share.

6. The minimum subscription as defined below, and where any part of the sums required for the matters set out in that definition is to be provided out of sources other than share capital, particulars of the amount to be so provided and the sources thereof.

The term 'minimum subscription' means the minimum amount which, in the opinion of directors, must be raised by the issue of share capital in order to provide for the property to be purchased, preliminary expenses and commission on shares, repayment of borrowed monies, and working capital.

7. The names of underwriters and the directors' opinion as to their financial resources.

8. Any commission payable on shares or debentures and any discount on shares.

5. Property Purchased.

1. The amount of the purchase consideration, specifying the amount paid for goodwill.

2. If any property purchased by the company has changed hands during the past two years, the amount paid by the purchaser thereof at each transfer. If the said property is a business, the profits of such business for the preceding three years together with a balance sheet as on a date not more than 90 days earlier. The statement of the three years' profits must clearly show the trading results and all charges and expenses incidental thereto *excluding* (a) profits not belonging to the period covered and (b) non-recurring profits, but *including* profits appropriated for taxation or reserves. This is a safeguard against inflation of assets; but to be effective there ought to be an accountant's report regarding profits and a valuer's report regarding assets.

6. Vendors.

1. The names and addresses of the vendors and the amount payable to each in cash, shares or debentures.

2. The number of shares and debentures agreed to be issued as fully or partly paid up otherwise than in cash, and the consideration for their issue.

For this purpose the term 'vendor' includes the lessor where the property is taken on lease.

7. Promoters.

The amount paid or intended to be paid to any promoter and the consideration for any such payment.

8. Preliminary Expenses.

*The amount or estimated amount of preliminary expenses.

9. Material Contracts.

The dates of and the parties to every material contract, and a reasonable time and place at which it may be inspected *except* a contract entered into in the ordinary course of the company's business. A material contract is one which is calculated to influence persons in making up their minds whether or not they may apply for shares.

Under section 99, the terms of these contracts cannot be altered without the consent of the company in general meeting.

10. Auditors.

The names and addresses of the auditors of the company, if any.

Voluntary Information. In a company prospectus, besides the information compulsorily required by law, the following information is usually included voluntarily:—Details of share capital and the terms on which shares and debentures are being offered for subscription; procedure as to how applications

for shares and debentures are to be made; a detailed statement about the company's prospects supported by facts and figures, business and technical qualifications of the company's directors and other officials closing of lists; and a statement that an application will be made to the Stock Exchange for permission to deal in the shares of the company.

Closing of Lists. When an intending investor applies for certain shares forwarding the amount required on application, he has to wait until the lists close before he knows whether the number for which he has applied will in fact be allotted to him. He may receive all he has asked for or he may only receive a portion.

The subscription lists cannot, of course, be closed before the minimum subscription has been applied for, but the promoters are not always scrupulous about their treatment of the lists. An announcement may sometimes be made that the lists closed on such and such day, the issue being heavily oversubscribed, when actually the undersubscribers have been left with a heavy portion of the share issue. The reason for this manoeuvring is simple. Any subscriber can withdraw his application while the lists remain open and before the directors have proceeded to allotment. If an issue is dragging, wise or timid applicants may hasten to withdraw their applications.

It must not, therefore, be supposed that the early closing of the subscription lists necessarily implies a prosperous future for the new company or even a steady and perpetual market in its shares.

Permission to Deal. It is usually announced on a prospectus that the company will apply for permission to deal in the shares on the Stock Exchange. Unless this permission is sought and obtained there will be, of course, no general market in the shares after they have been allotted. Permission to deal is by no means granted indiscriminately, and new issues are carefully scrutinised by a special committee of the Stock Exchange before such permission is granted. When permission to deal has been granted, the names of the securities will appear in the official lists, of business done and all bargains that have been entered by the brokers will be recorded.

The opinion is unfortunately widely prevalent that just because a company has its shares quoted on the Stock Exchange, it thereby acquires a certain measure of soundness and promise of prosperity. The fact of the matter is that, if normal listing requirements are complied with, the Stock Exchange automatically permits dealings in shares of any company, sound or unsound, for it cannot profess to sit in judgment on the inherent soundness, much less the future prospects, of a new company.

(b) Prospectus issued by a company already carrying on business

The matters marked with an asterisk (*), which are required to be disclosed in the prospectus of a newly-incorporated company, are not required to be stated in the prospectus of an existing company if the prospectus is issued more than one year after the date on which the company became entitled to commence business.

But the prospectus issued by a company which has been carrying on business prior to the issue thereof must contain the following *additional* information :—

1. The amount of shares offered on each previous allotment within the past two years and the amount paid on the shares allotted.

2. Any commission on shares or debentures and any discount on shares paid during the past two years, stating separately the amount so paid to managing agents.

3. The number of shares and debentures issued within the past two years as fully or partly paid up otherwise than in cash, and the consideration for such payment.

4. The amount paid within the past two years to any promoter and the consideration for such payment.

5. The dates of and the parties to every material contract, and a reasonable time and place at which it may be inspected *except* (a) contracts entered into in the ordinary course of the company's business and (b) contracts made more than two years previously, which are not in connection with the appointment and remuneration of managing director or managing agents.

6. An auditor's report and an accountant's report as explained below.

Auditor's Report. The report of the company's auditor must deal with the following matters :—

(a) The profits of the company for each of the three financial years immediately preceding the issue of the prospectus, supported by a properly classified profit and loss account showing clearly the trading results and all charges and expenses incidental thereto excluding profits not belonging to the period covered and non-recurring profits, but including profits appropriated for taxation or reserves ;

(b) The rates of dividends (if any) paid by the company for each of the three years stating the particulars of each class of shares on which dividends have been paid, that is to say, the total paid-up share capital and the total number of the issued shares of each class together with the amount of each share ; the source from which dividends have been paid ; and the particulars of the cases in which no dividends have been paid on any class of shares.

If the latest available audited accounts of the company are more than three months old on the date of the prospectus, a statement of that fact must be included in the auditor's report : and if the company has been carrying on business for less than three years and its accounts have been made up only for two years or less, then the auditor's report need be confined only to that period.

Where the company has a subsidiary company, similar information relating to the subsidiary company must also be included in the auditor's report.

The purpose of this report is to enable the investor to judge by past results of the company what the company may be expected to do in the future. It is true that a report on past profits and dividends gives some idea as to remunerative

character of the undertaking, but it is no guide to the financial position of the company which can only be ascertained from its balance sheet, which is, of course, not to be given in the prospectus. There may be mortgages and charges on the company's assets, there may be heavy contingent liabilities, or there may be bad debts for which adequate provision may not have been made. The depreciation provided for may be inadequate and consequently the book account may be inflated. The working capital of the company may be insufficient. All these things which so vitally affect the judgment of the intending investors with regard to the financial condition of the company can only be ascertained from the company's balance sheet. It is, however, open to the investors to procure a copy of the company's last published balance sheet in other ways.

Accountant's Report If the proceeds of an issue of shares or debentures are to be applied directly or indirectly in the purchase of any business, report by a registered accountant upon the profits of the business intended to be purchased, for each of the three financial years immediately preceding the issue of the prospectus, must be set out in the prospectus.

This report must also be supported by a properly summarised profit and loss account of the business to be purchased showing clearly the trading results and all charges and expenses incidental thereto excluding profits not belonging to the period covered and profits of a non-recurring nature, but including profits appropriated for taxation or reserves.

The object of this report is to enable those, who intend to purchase the shares or debentures of the company issuing the prospectus, to ascertain the profit-earning capacity of the business which is to be purchased by the company with the proceeds of such shares or debentures. Under section 93 (1) (f), it is also necessary that the balance sheet of such business, made up to a date not more than ninety days before the date of the prospectus, should be included in the prospectus of the company; but it is not legally necessary, although it is desirable, that such balance sheet should be audited by the accountant. In practice, however, when an accountant is asked to report on the profits of the business for the three previous financial years, he may also be asked to report upon its balance sheet in order to make it authentic from the point of view of prospective investors.

(c) Prospectus issued by a private company on becoming public

When a private company wishes to become a public company, it is required to make the necessary alterations in its articles of association in accordance with the provisions of section 154, and is also required to file a prospectus or a statement in lieu of the prospectus with the Registrar. The prospectus to be issued by such a company must contain all the particulars required to be disclosed in the prospectus of a newly incorporated company *except* the amount or estimate of preliminary expenses.

(d) Prospectus issued by a foreign company

The law governing the circulation in British India of the prospectuses of

companies registered outside British India is contained in section 277, 277.A, 277.B, and 277.C.

It shall not be lawful for any person (a) to circulate in British India the prospectus of a foreign company, whether it has established a place of business in British India or not unless it contains the prescribed information ; and (b) to issue to any person in British India a form of application for shares or debentures of such a company unless the form is accompanied by a prospectus.

The prospectus of a foreign company, before it is circulated in British India, must comply with the following requirements, in addition to the information that it must contain in accordance with the law in force in the country or state in which the company has been incorporated :—

1. It must be dated, a certified copy thereof delivered to the Registrar of a province in British India for registration, and this fact stated on the face of it.

2. It must contain particulars with regard to :—

* (a) The objects of the company, or only the primary object of the company if the prospectus is published as a newspaper advertisement ;

* (b) The instrument constituting or defining the constitution of the company ;

* (c) The law under which the company is incorporated ;

(d) An address in British India where the said instrument of law or copies thereof can be inspected ;

(e) The date on which and the country in which the company was incorporated ;

(f) Whether the company has established a place of business in British India and, if so, the address of its principal office in British India ;

Provided that the items marked with an asterisk need not be given if the prospectus is issued more than two years after the date on which the company was entitled to commence business.

3. If the prospectus is issued by a company already carrying on business it must contain the auditor's report and the accountant's report as required by section 93 (IA), *i. e.*, as in the case of a company registered in British India.

4. If the liability of the members of the foreign company is limited, the prospectus must indicate that fact.

5. It is not lawful for any person to go from house to house offering shares of a company incorporated outside India for subscription or purchase to the public or any member of the public.

Note.—If a form of application is issued to an underwriter, it need not be accompanied by a prospectus. The above provisions do not apply to a prospectus or a form of application issued to existing members of the company. An offer for sale of the shares or debentures of a foreign company to the public (but not to a professional stock broker) is deemed to be a prospectus.

The object of these provisions is to prevent the sale of worthless securities of foreign companies in this country. Besides there is dearth of money in our own country and every rupee can well be utilised for advancing our own industries. Before the enactment of these provisions in 1936, a considerable amount of business was being carried on in India in the shares and bonds of foreign companies. Growing accounts were usually given by the canvassers and the agents employed by these companies of the profits likely to be made by investing money in such commodities. The unwary investors not acquainted with the details of foreign corporations were very often trapped, and in most cases lost all the monies which they had invested in the purchase of such securities.

Statement in Lieu Prospectus. If a public company does not issue a prospectus on its formation, it must file a statement in lieu of prospectus in the prescribed form, before it can allot any shares or debentures. The object of this provision is to secure in the Registrar's office some essential information about the company.

Offer for Sale. A company may allot or agree to allot its shares or debentures to another company, firm or person, with a view to that company, firm or person offering the shares or debentures so allotted to the public. The document offering the shares or debentures to the public is generally called an "Offer for Sale". This document, is, under section 92-A, deemed to be a prospectus issued by the company, i. e., the company that originally allots or agrees to allot the shares or debentures.

The following is a summary of the main requirements with regard to offers for sale :—

1. All matters which must be included in a prospectus must be included in an offer for sale.
2. A copy of the offer for sale must be dated and filed with the Registrar like a prospectus, and must be signed by the persons making the offer. If the offer is made by a company, the offer for sale must be signed by not less than two directors; if the offer is made by a firm, then by not less than half the partners.
3. In addition to the matters required to be stated in a prospectus, an offer for sale must include (a) the net amount of consideration received by the company in respect of the shares or debentures to which the offer relates, and (b) the place and time at which the contract for the allotment of the said shares or debentures may be inspected.

The form of an offer for sale generally follows that of a prospectus, and the additional information referred to above may be conveniently inserted in any part of the document.

Announcement. The legal definition of the term prospectus, as given in section 2 (14) exempts trade advertisements from the rigours of a prospectus. From the point of view of intending investors, this is a weakness of the law. It is true that a trade advertisement, which is intended to bring to the notice of

the public shares and debentures of a company available for sale, must show on the face of it that a formal prospectus has been prepared and filed : but this in itself constitutes no real safeguard for the investing public, since there are no restrictions as to the contents of such advertisements.

It is open to any person to offer shares or debentures by inserting in the advertisement exaggerated or misleading statements pertaining to the company. He may in fact insert matters which have not been disclosed in the prospectus or omit those which are given in the prospectus. In effect therefore such advertisements (or announcements as they are usually called) serve as an invitation to the public to subscribe for shares on the faith of misleading or exaggerated statements contained therein, although on the top of such announcements a statement such as the following usually appears : "This is not a prospectus, but simply an announcement."

Moreover during the present boom in company flotations, a very number of such announcements have appeared in the press, in which even there is no indication that a formal prospectus has been prepared and filed. It may be that such companies may not have issued any prospectus at all. In any case the so called announcements, which do not come within the definition of a prospectus, are against the interests of the investors.

Control of Capital Issues

The control of capital issues came into force in British India for the first time in May 1913, purely as a war-time measure, under the Defence of India Rule 94-A, which expired at the end of September 1946. It was then continued under a special ordinance of the Central Government, which has been replaced by the Capital Issues (Continuance of Control) Act of 1947.

The Act for the control of capital issues prohibits, without the sanction of the Central Government, an issue of capital in British India ; and it also prohibits an issue of capital anywhere (whether within or without British India) by a company incorporated in British India. No person is allowed to issue, in British India any prospectus or other document offering for sale any security which has not the prior sanction of the Central Government and a statement to this effect. No person shall subscribe for any securities issued by a company unless such issue has been made with the consent of the Central Government.

The provisions of the Act governing the control of capital issues do not, however, apply in the following cases :—

(a) Where the issue of capital does not exceed Rs. 5 lakhs except in the case of banking and insurance companies ;

(b) Where securities are issued by persons in the ordinary course of their normal business and solely for the purpose of that business to a banker in respect of advances ;

(c) Where non-Indian concerns established in Indian State raise capital outside British India ; and

(d) Where forfeited shares are reissued.

If any promoter, managing agent or subscriber contravenes the provisions of the Act, he is liable to imprisonment for a period which may extend to one year or to fine, or to both.

If a company desires to secure the government's sanction for the issue of capital, it must make an application in the prescribed form to the Government of India. It is then thoroughly examined by a committee of the Finance Department. Applications from banking and insurance companies are also examined by the Reserve Bank of India and the Superintendent of Insurance respectively. If all the conditions are fully satisfied, the Central Government gives its sanction.

All capital issues sanctioned by government are made known to the public every week by means of a classified statement showing consent to issues of new companies and those of existing ones separately. This information should enable investors to decide in advance about the choice of their investments; and it should also enable enterpreneurs to know whether anyone else has entered the field of activity contemplated by them.

The conditions on which sanction is given by the Central Government to the issue of capital are required to be stated on the prospectus or other invitation to the public. The usual form of the statement where no special conditions are insisted upon by the Government is "Consent of the Central Government has been obtained to this issue of capital; but it must be distinctly understood that in giving this consent the Government of India do not take any responsibility for the financial soundness of any scheme or for the correctness of any of the statements made or opinion expressed with regard to them."

The object of government in instituting the control of capital issues was primarily to meet an emergency by preventing the growth of mushroom companies, by checking inflation, by giving priority to munitions production, and by diverting surplus public savings directly or indirectly into public treasuries as subscriptions to war loans. The main objective of this control has been to prevent a scramble for the limited supplies of most essential goods and services. It aims at checking the undesirable practices such as the reconstitution and recapitalisation of concerns on the basis of their abnormal profits to the detriment of an indiscriminating investing public. There has been no intention of handicapping or retarding sound and legitimate industrial development. It has been rightly emphasised "that the object of the capital issue control is to secure a balanced investment in industry, agriculture and the social services, and to ensure that the available capital resources are utilised on a balanced plan of agricultural, industrial and other development and to keep a balance between the manufacture of capital and consumer goods."

The principles governing the grant of sanction for the issue of capital are as follows :—

(a) The promoters, directors, and their friends and relatives are required to take up at least one-fifth of the capital proposed to be raised, and a prospectus cannot be issued until this amount has been subscribed by them.

and the balance in two calls of Rs. 25 each per share at intervals of not less than two month between each call.

The Government of the Central Provinces and Berar have subscribed for cash 1,50,000 Ordinary Shares of Rs. 100 each of the value of Rs. 1,50,00,000 which will be allotted in full and 5,000 Ordinary Shares of the value of Rs. 5,00,000 (five lakhs) will be issued as fully paid up to the Government of C. P. and Berar in consideration of the facilities granted by them to the Company and provided in the agreement referred to hereinafter.

The signatories to the Memorandum, the Directors, the Managing Agents and their friends have subscribed for cash 25,000 Ordinary Shares of the value of Rs. 25,00,000 and the same will be allotted fully.

The remaining 1,25,000 $\frac{1}{2}$ per cent. Redeemable Cumulative Preference Shares of Rs. 100 each and 70,000 Ordinary Shares of Rs. 100 each are now offered to the public for subscription. Preference to the extent of 40 per cent. of the shares offered to the public will be given to applications received from residents of C. P. and Berar.

The Redeemable Preference Shares in the Company will confer the right to a fixed cumulative preferential dividend at the rate of five and a half per cent. per annum (taxable) on the capital for the time being paid up thereon and the right in a winding-up to the payment of all arrears of dividend whether earned or declared or not down to the commencement of the winding-up and also to repayment of capital paid-up or credited as paid-up on the Preference Shares held by them respectively in priority to any payment in respect of Ordinary Shares, but shall not confer any other right to participate in profits or assets of the Company. The Preference Shares will be redeemable at any time after 1st January, 1963, at par at the option of the Company on giving six months' notice. The said Preference Shares will rank for dividend on and after the date of the certificate for commencement of business on the capital for the time being paid up thereon.

Subject as aforesaid and to the rights of the holders of any other shares entitled by the terms of issue to preferential payment over the Ordinary Shares, in the event of winding-up of the Company the holders of the Ordinary Shares shall be entitled to be repaid the amount of the capital paid-up or credited as paid-up on such shares and all such surplus assets thereafter shall belong to the holders of the Ordinary Shares in proportion to the amount paid up or credited as paid up on such Ordinary Shares respectively at the date of the commencement of the winding-up.

Directors :

1. Sir M. B. Dadabhoy, K.C.S.I., K.C.I.E., Kt., LL.D., Chairman. Chair-
man and Managing Director : The Model Mills Ltd, The Berar
Manufacturing Co., Ltd., The Nagpur Electric Light and Power Co.,
Ltd., Managing Proprietor : Ballrapur Collieries. Proprietor : New
Chirimiri Ponri Hill Colliery, etc., Henessy Road, Nagpur.

2. Sir Jnan Chandra Ghosh, B.Sc., F.N.I., Director General, Industries and Supply, Government of India, New Belhi.
3. Raja Bahadur Virendra Bahadur Singh, Ruler of Khairagarh State. Director : The National Newsprint and Paper Mills Ltd., The Jagharkhand Mines Ltd., etc., Virendra Bhawan, Khanagarh, C.P.
4. V. Seshasayee, Esq., Managing Director : Mettur Chemicals & Industrial Corpn. Ltd. Seshasayee Bros., Ltd., Fertilisers and Chemicals Travancore Ltd., Trichinopoly.
5. S. B. Butt, M.A., Ph.D., (Econ) (Lond) Barrister, Managing Director, The Comilla Union Bank Ltd., Director : Hindusthan General Insurance Co., Ltd., East India Insurance Co., Ltd., etc., 12 Earle Street, Calcutta.
6. Prof. S. K. Roy, M.E.E. (Harvard), M.A.I.E.E., M.I.E. (India), Director : The Bengal Electric Lamp Works Ltd., The Bengal Belting Works Ltd., etc., etc., P. O. Jadavpur College, 24 Parganas.
7. K. A. Narain Rao, B.Sc. (Lond) F.R.I.C., Director of Industries and Secretary to Government of C. P. and Berar, Civil Station, Nagpur, C. P.
8. Lt.-Col. E. G. Mackie, M.A.I.E.E., M.I.M.E., A.I.E.E., Chief Electrical Engineer and General Manager, Electricity Department, Government of C. P. and Berar, 14, Telankheri Road, Nagpur, C. P.
9. Seth Mathuradas Mohita, Managing Director : R. S. Rockchand Mohita, Spinning and Weaving Mills, Hinganghat, C. P.
10. Ramesh Madho Rao Deshmukh, Prime Minister, Rewa State, Rewa, C.I.
11. Mr. Walter Dutt, Barrister-at-Law, 5, Mayo Road, Allahabad.

Managing Agents :

Hind. Alco Limited, St. A, Nerbudda Road, Jubbulpore.

Bankers :

The Imperial Bank of India, Head Office, Bombay.

The Central Bank of India Limited, Mahatma Gandhi Road, Bombay.

The Comilla Union Bank Ltd., 4, Netaji Subhas Road, Calcutta.

Solicitors :

Messrs. Mulla & Mulla, Solicitors and Notary Public, 51, Mahatma Gandhi Road, Bombay.

Brokers :

K. U. Advani, Aga Khan Bldg., Balal Street, Bombay.

Swastik & Co., Madras.

Kishan Chand Jhunjhunwala, 7, Lyons Range, Calcutta.

Auditors :

S. B. Billimoria & Co., 113, Esplanade Road, Bombay.

Batlibhoy and Purohit, 204, Hornby Road, Bombay.

Registered Office :

84-A Nerbudda Road, Jubbulpore.

PROSPECTUS

Objects

The Company has been formed for the objects mentioned in the Memorandum and particularly for the manufacture of Alumina, Aluminium Metal and Aluminium Compounds at Katri, C. P.

Need for Aluminium

Aluminium has rightly been called the "wonder" metal of this age. Its amazing lightness, ductibility, malleability, its high degree of resistance to corrosive and chemical action, high electrical and thermal conductivity and its ability to form high strength alloys in conjunction with other metals have led to its widest possible application in all departments of industry and civilised life during peace time as well as war.

The Report of the Industrial Panel on Non-Ferrous Metal Industries published by the Government of India Planning and Development Department states :—

"We cannot lay enough stress on the importance of increasing the production and use of aluminium in India. There is an abundance of raw materials available for the production and since India is known to be deficient in ores of other industrial metals like copper, zinc, lead, tin, etc., it is obvious that the future of Indian industry is bound up with the development of its aluminium industry. Aluminium and its alloys can be easily with advantage substituted for most of the other non-ferrous and ferrous materials" (vide page 25).

"We have set the minimum target for average annual production for the first five years at 15,000 tons and feel that this production can be easily realised, by starting new reduction works" (vide page 26).

The Report of the Heavy Chemicals and Electro-Chemical Industries Panel published by the Government of India states :

"(Para 29.) It is difficult to foresee the demand in future industrial India. With the development of the engineering industries estimates have been put up as high as 20,000 tons which may not be improbable considering the large developments electrical, technical and chemical, planned. As regards demand for utensils, even if we plan on the basis of one plate and one tumbler per head for half of India's population, the demand for aluminium will be very large. Since Indian resources of copper and zinc are very scanty, we are of the opinion that aluminium should be utilised in a greater degree for utensils. We understand that if metal of sufficient purity is used, the utensils are not corroded by highly spiced food. Transport services could consume the metal in large quantities. Taking all these into consideration we recommend that production should be raised to 15,000 tons per annum immediately, with provision for 20,000 tons later. Government of India are therefore requested to make arrangements for another aluminium plant of 5,000 tons immediate capacity ultimately to be raised to 8,000.10,000 tons near a source of power supply."

In view of the recommendations of all these expert bodies there can be no doubt as to the urgent need for considerable increase in the present production.

of aluminium in India by the establishment of new factories.

Raw Materials

Extensive reserves of suitable bauxite exist in the Jabulpore District. Sir Cyril Fox, D.Sc., F.G.S. M.I.Min E., late Director, Geological Survey of India, while making a report on these resources writes :—

"The material is readily soluble in caustic soda, even more so than the best type areas of France, and thus suitable for treatment by the Bayer process for the preparation of Alumina. It requires roughly 2 tons of Bauxite to yield one ton of Alumina suitable for reduction to Aluminium. Indeed one ton of Aluminium requires two tons of Alumina. Therefore, four tons of raw bauxite will yield 1 ton of Aluminium. Therefore, an output of 10,000 tons of Metallic aluminium means the preparation of 20,000 tons of Alumina and a supply of 40,000 tons of Bauxite. At this rate reserves of 5 million tons of Bauxite would provide for 125 years. I have no hesitation in saying that the country south and south-west of Katni could maintain the above production (40,000 tons annually) for 125 years and probably much longer if all the deposits were under monopolistic control." (A complete copy of the original report can be seen at the Registered Office of the Company.)

Coal is abundantly available. The alumina and chemical by-product plants will require 20,000 tons of coal per annum and at present it is also proposed to produce power from a Thermal Power Plant but in later years the Government visualises the possibility of supplying power to the company at a very cheap rate from hydro-electric projects and has agreed to take over the company's thermal power plant in such eventuality at the full cost less depreciation at 5 per cent. per annum.

Cryolite, Petroleum Coke and Pitch are available. The Company will manufacture its own carbon electrodes. A Caustic Soda plant is planned and has been negotiated for.

Machinery

The Company has secured a complete power plant in Switzerland specially designed for the production of aluminium metal and two-thirds of the price has been paid to the manufacturers by the Government. The machinery is expected to reach India by the end of 1918. The machinery for the Alumina plant, the reduction works and the rolling mills has been negotiated for and is promised for delivery within a short time.

Technical Co-operation

The Managing Agents have obtained an agreement for full technical co-operation from Societe Anonyme pour l'Industrie de l'Aluminium of Lausanne, Switzerland who are the leading manufacturers of Alumina and Aluminium in Europe. The Swiss Company will send their experts to India for working the plants and also train our personnel in their works in Europe.

The Managing Agents have negotiated an agreement with Dorr Engineers Inc of New York, U.S.A. for designing, and erection of a Bayer Process Alumina Plant.

The Managing Agents have further obtained an agreement from Mr. L. Gupta, M. Sc., F.I.C.S., consulting chemist, for full co-operation and working of the chemical plants to be established by the Company.

Provincial Government's Support

The Government of C.P. and Berar have 51 per cent. share in the Managing Agency and further have agreed as follows :—

- (i) To invest one crore and fifty lakhs of rupees in Ordinary Share capital of the Company.
- (ii) To nominate three persons to act as Directors of the Company.
- (iii) To acquire the proposed site for the Company.
- (iv) To construct necessary roads.
- (v) Not to charge any tax or cess for water used by the Company.
- (vi) To arrange for a suitable railway siding at the proposed site.

Government of India's Support

The Government of India have carefully examined the scheme and have assured the Provincial Government of their full co-operation and assistance to make the venture a success and have further nominated the Director General, Industry and Supply, to act as a Director on the Board of Directors of the Company.

Proposed Site

An extensive plot of ground adjacent to the B. N. Ry. line about one mile from Katni town has been chosen as the site for the proposed industry. The land is very suitable for building and has excellent road and railway connections and is supplied with a perennial source of water from a near-by river. (See Map).

Taking all the above factors into consideration the Directors feel that the Company will be able to pay a reasonable dividend to the Shareholders.

Promoters

The Government of C.P. and Berar and Mr. Walter Dutt are the promoters of the Company. The promoters have negotiated all matters relating to the formation and registration of the Company. The promoters as such will not receive any remuneration for their services.

Preliminary Expenses

The Managing Agents will be entitled to be repaid all sums expended and to be indemnified against all liabilities incurred. The preliminary expenses (excluding the underwriting commission and brokerage) it is estimated will not exceed rupees two lakhs.

Minimum Subscription

The minimum subscription upon which the Directors may proceed to allotment and which in the opinion of the Directors must be raised out of the proceeds of this issue for the matters specified in Section 101 (2) of the Indian Companies Act VII of 1913 including the working capital is rupees two crores.

Agreements

The following contracts will be entered into by the Company :—

- (i) Managing Agency Agreement between Hind.Alco Ltd., and the Company.
- (ii) Sale Contract in respect of bauxite with the option to purchase the mining rights in certain specified areas between the Company and Mr. Walter Dutt.
- (iii) An agreement between the Government of C.P. & Berar and the Company granting certain facilities to the Company, and providing for investment of one crore fifty lakhs rupees by Government in the capital of the Company.

Interest of Directors in Agreements

The following Directors are interested in the Contracts :—

- (i) Mr. Walter Dutt as vendor of the bauxite ore and properties mentioned in the sale contract and as a shareholder and director of the managing agents firm in the managing agency agreement.
- (ii) Prof. S. K. Roy, in the managing agency agreement being a shareholder and director of Hind.Alco Ltd.

Director's Qualification and Remuneration

The Articles of Association provide as follows :—

- Art. 91. "The qualification of a director shall be the holding of at least 250 Ordinary Shares in the Company but in the case of an ex-officio director appointed by Government the appointment shall be made by his official designation and shares necessary for his qualification may be held by Government."
- Art. 93. "The directors shall be paid out of the funds of the company such fees not exceeding Rs. 100 for each director as they may from time to time fix for each meeting of their Board attended by each of them. The directors shall also be entitled to be paid their reasonable travelling and hotel and other expenses incurred in consequence of their attendance at Board meetings"
- Art. 94. "If any director being willing shall be called upon to make any special exertions in going or residing abroad, or otherwise for any of the purposes of the Company, the Company shall remunerate such director by a fixed sum or otherwise as may be determined by the directors and such remuneration may be in addition to or in substitution for his fees and remuneration above provided."

Powers of Directors

No restrictions are imposed by the Articles of Association on the directors' powers of management and control of the Company's affairs is vested in the directors. The powers of the directors are, however, subject to any regulation not being inconsistent with the Articles of Association and the Indian Companies Act, which may be made by the Company in general meeting.

Appointment of Managing Agents and their Remuneration

The articles of Association and the Agreement with the managing agents provide that Hind. Alco Limited shall be the managing agents of the Company for a period of twenty years commencing from the date of incorporation of the Company.

Subject to the provisions of the Indian Companies Act, the managing agents are entitled under the terms of the agreement to receive by way of remuneration for their services a commission of ten per cent. of the net yearly profits of the Company but subject to a minimum payment of Rs. 3,500 per month.

The said remuneration shall be exclusive of payments to the Bankers, Solicitors, Commission Agents, dealers, mukadams, brokers, officers or employees who may be employed by the managing agents for and on behalf of the Company or for carrying on and conducting the business of the Company.

Under the terms of the Agreement the managing agents are entitled to nominate two directors to the Board.

~~A~~ Voting Power

Subject to any special rights or restrictions as to voting upon which any shares may be held, on a show of hands every member present in person and being a holder of Ordinary Shares (or by General Proxy who is not a member of the Company or is not a member qualified to vote) shall have one vote. Upon a poll every member present in person or by proxy shall have one vote for every Ordinary Share held by him. The Preference Shares do not confer any voting rights but holders will be entitled to be present at any meeting of the Company.

~~A~~ Restriction on Rights to Transfer and Vote

Directors may decline to register the transfer of shares upon which the Company has a lien, and in the case of shares not fully paid up may refuse to register a transfer to a transferee of whom they do not approve. The Company has no lien on fully paid up shares.

~~A~~ Brokerage

Brokerage at the rate not exceeding rupee one per cent. of the nominal value of the shares will be paid by the Company on allotment made in respect of applications bearing the stamp of any recognised broker or brokers in respect of the shares not underwritten.

~~A~~ Commission

The Company may pay a commission in any person in consideration of his subscribing or agreeing to subscribe (whether absolutely or conditionally) for any shares in the Company or procuring or agreeing to procure subscriptions (whether absolute or conditional) for any shares of the Company at the rate of not exceeding three per cent. on the shares in each case.

~~A~~ Documents

Copies of the Memorandum and Articles of Association and the originals of the Agreements referred to above can be inspected at the Registered Office of the Company and copies of all the documents may be inspected at the offices of the Company's brokers during the usual business hours.

Application for Shares

An Application for shares should be made on the appropriate form and sent to the managing agents or to the Company's bankers together with a remittance of the amount payable on application. Where no allotment is made the deposit will be returned in full and where the number of shares allotted is less than the number of shares applied for the balance of the deposit after providing for payment in full on the shares allotted will be returned.

Copies of the Prospectus and forms of application for Ordinary Shares and for Redeemable Preference Shares may be obtained from the managing agents or the Company's bankers or their Branches or from the Company's brokers.

M. B. Dadabhai
J. C. Ghosh
Virendra Bahadur Singh
V. Seshasayee
S. B. Dutt
S. K. Roy
K. A. N. Rao
D. G. Mackie
Mathuradas Mohita
R. M. Deshmukh
Walter Dutt

} *Directors*

Dated the 25th April, 1948

Application For Shares

THE NATIONAL ALUMINIUM COMPANY OF INDIA LIMITED.

(Incorporated at Nagpur under Indian Companies Act, 1913.)

To

The Directors,

The National Aluminium Company of India Ltd.,

84A, Nerbudda Road, Jabalpur (C. P.)

Gentlemen,

I enclose herewith cash/cheque for the sum of Rupees being the application deposit at Rs. 25 per share on Ordinary/Preference Shares of Rs 100 each in your Company and request you to allot to me/us the said number of shares or any lesser number, subject to the terms and conditions of the Memorandum and Articles of Association of your Company. I/We agree to pay Rs 25 per share on allotment and the balance in two equal calls and I/we hereby authorise you to place my/our name in the Register of Members in respect of the shares allotted.

IN
BLOCK
LETTERS

Usual Signature
Name
Occupation
Address

Station

Date

~~A~~ N.B.—This form with remittance must be sent entire to the company direct or to the Company's Bankers at any branch.

THE NATIONAL ALUMINIUM COMPANY OF INDIA LIMITED.

Receipt For Application Deposit.

No. Dated 194 .

Received from by Cheque/Cash the sum of Rs. subject to realisation, being a deposit of Rs. 25 per share on application for Ordinary/Preference Shares in the abovenamed Company.

Rs.

N.B.—This receipt must be preserved to be exchanged hereafter for share Certificate.

Consequences of Omissions

If a prospectus does not comply with the requirements of law, those responsible for its issue are liable to a fine up to Rs. 50 a day so long as the default continues; and further section 93 (6) provides that nothing in this section shall limit or diminish any liability which any person may incur under the general law.

A person, who buys shares or debentures on the faith of a prospectus which does not contain all the statutory information, has no right to rescind the contract to take shares or debentures, nor has he any other remedy against the company. However, if he has suffered any loss he may have a right of action for damages against the promoters, directors or other persons responsible for the issue of the prospectus; but a director, etc., can escape liability by proving (a) that he was not cognisant of the matter omitted; or (b) that non-compliance or contravention arose from an honest mistake of fact on his part; or (c) that the non-compliance or contravention referred to matters immaterial or was such as may reasonably be excused.

Where material facts are omitted, such omission may sometimes amount to misrepresentation or fraud, the consequences of which are explained below.

Consequences of Misrepresentation or Fraud.

The object of issuing a prospectus is to induce the public to subscribe for shares or debentures of the company; therefore the persons issuing it naturally desire to make it as attractive as possible to the prospective investors. But it is very important to remember that a prospectus should never be misleading. It should reveal the facts in their true colour, because investors put their money in the company on the faith of its prospectus. If a prospectus contains any misleading untrue statements, those responsible for its issue must take the consequences.

In considering what is misrepresentation, it is necessary to tell not only the truth, but all the truth, and that concealment of facts may easily imply falsehood and may possibly amount to fraud. The Royal Mail prosecution bears out this point. It will be remembered in this case that, although certain statements

were made, yet material facts qualifying those statements were withheld.

Where there is an untrue statement of a material fact in a prospectus, on which the applicant relied at the time of subscribing for shares or debentures, he has two remedies, viz.—

1. *Right of Rescission.* In the first place, the subscriber who has applied for shares is entitled under the general law (i. e., the law of contract) to apply to the Court for rescission of the contract. Such a contract is not void but voidable at the option of the subscriber to the company's shares. Under section 19 of the Indian Contract Act, the contract would not however be voidable if the plaintiff had the means of discovering the truth with ordinary diligence.

On application to the Court the shareholder is entitled to have his name removed from the register of members of the amount paid upon the shares or debentures returned to him with interest.

A person who takes shares not from the company but from another shareholder has no remedy against the company. But this rule will not apply where the prospectus is intended and used to induce purchasers in the market to buy the shares.

The right of rescission against the company is, however, lost in the following cases :—

- (a) If the shareholder does not take action within a reasonable time after the untrue statement has come to his knowledge ;
- (b) If he impliedly ratifies the voidable contract after he has knowledge of any untrue statement, e. g., trying to sell his shares, paying calls, receiving dividends or voting at meetings ;
- (c) If the company goes into liquidation before the right of repudiation is exercised, because on the winding up of the company the rights of creditors intervene to prevent the company being rescinded.

2. *Right of Action for Damages.* Where the right of rescission is lost, the injured party has still a right of bringing an action for damages against those responsible for the issue of the prospectus, and this right is available even after a company has gone into liquidation.

Section 100 provides that a director or promoter is liable to compensate any persons who subscribe for shares or debentures on the faith of the prospectus for loss or damage sustained by them on account of any misleading or untrue statement appearing therein. The following defences are, however, open to a person sued for damages :—

- (a) That he had reasonable ground for believing the statement to be true ;
- (b) That he made the statement on the authority of an expert whom he believed to be competent ;
- (c) That the statement was a correct copy of some extract from an official document ;
- (d) That he withdrew his consent to the issue of the prospectus or that he never gave his consent to its issue ;

- (e) That the prospectus was issued without his knowledge and that on knowing the fact he gave a public notice that it was issued without his knowledge ;
- (f) That after the issue of the prospectus but before the allotment thereunder he on knowing the untrue statement withdrew his consent and gave a public notice.

The action for damages must be taken within three years after the allotment of shares. The amount of damages would be assessed by the Court and may be the difference between what the shares are worth and what they would have been worth had the statement been true.

A promoter or director who pays damages to a shareholder is entitled to a *pro rata* contribution from his co-promoters or co-directors who would have been liable in damages, and the ordinary rule of law that there shall be no contribution between joint wrong-doers does not apply.

Further the estate of a person who is liable under section 100 before death is not liable unless it has benefitted by a misrepresentation in the prospectus.

How to Read a Company Prospectus.

From the point of view of prospective investors, the prospectus issued by a company is an important document. Every new company may be regarded as a three legged horse, and the purpose of the prospectus is to persuade the public that it has four legs. To quote Mr. W. Collin Brooks from his book "*Theory and Practice of Finance*," "We may safely regard every prospectus as a document drawn up in a mood of apparent ecstatic philanthropy by a champion optimist, with a view to extracting money from the pockets of others. When governments or public bodies of high repute invite loans, their solicitations are couched in restrained and dignified language, but the ordinary company inviting the public to subscribe money to its purposes develops a tendency not only to call all its gossamer wings but to mount all its chickens before the eggs from which they are to be hatched have even been laid."

Although the Indian company law as relating to company prospectuses has been considerably tightened up by the Indian Companies (Amendment) Act of 1936, yet it cannot still be considered fool-proof. In India where the public press is not equipped to give a lead to the investing public and where the public are in investment matters more ignorant than their compeers in other countries, the strictest regulations are necessary for safeguarding the unwary against the wiles of plausible company promoters. Prospectuses with high-sounding promises are largely circulated through private channels and are feelingly recommended by adroit share-pushers. It is, therefore, very necessary that investors should study a company prospectus with the utmost caution.

The following are the principal matters which should be carefully noted in examining a company prospectus :—

1. Nature of Business and its Prospects. Note the nature of business which the company is going to do and its likely prospects in the light of possible

competition, supply of labour and raw materials, markets, location of works, adequacy of equipment, and any tariff problem. The statements appearing in the prospectus with regard to these matters are usually optimistic. Allowance should therefore be made for such optimism and also for a little exaggeration. It should be remembered that the promoters, in drafting the prospectus, usually suffer from the great weakness, experienced by all persons who have anything to sell, of making the utmost of their wares.

A prospectus which relies largely on stating the successes that others have achieved in the same line of business should be taken with a grain of salt. The essential for success is not what others have been able to do but what the new concern is able to do and in whose hands the doing is placed.

2. Management. This usually consists of directors and managing agents. With regard to directors, ascertain their qualifications, their remuneration, their stake in the company and their powers *vis-à-vis* the managing agents. Nothing is more important in any prospectus than the names of directors. They need not be famous names. What the investor should make sure about is that the directors are men who have made a success in the type of business they are to control. It is equally important to ascertain whether most of the powers of directors have been usurped by the managing agents and whether there are any restrictions imposed by the articles on the powers of directors.

In the case of managing agents, find out if they are experienced in the line of business which the company is going to do, or are they merely newcomers in the field. Are the powers entrusted to them and the remuneration payable to them reasonable having regard to the nature of the company's business?

3. Capital Plan. This is a very important matter on which the success or failure of the company will largely depend. Is the amount of capital which the company is going to raise sufficient for its immediate requirements both in regard to block and working finance? Is the capital plan sufficiently elastic to permit the raising of further capital in future?

If the company is offering shares of different classes, see that the respective rights as regards dividend, repayment of capital, voting, etc., attached to them are reasonable, and that the proportion between the fixed-interest capital and the equity capital is satisfactory. A good capital plan is one which is simple and carefully devised.

Is the amount of minimum subscription adequate, because to start business with insufficient capital is to invite disaster? If any funds are to be raised otherwise than by share capital, note the sources thereof.

In case the issue has been underwritten, it is essential that the underwriters must be men of financial standing and the terms of the underwriting commission reasonable. See if any part of the issue is underwritten firm.

4. Property Purchased. Ascertain the nature and value of the property to be purchased by the company, the reasonableness of the price and how it is to be paid. If the property is a business, note the nature and value of the assets

being acquired, the price (if any) attributable to goodwill, the status of the vendors, the total amount of the purchase consideration and the way in which it is to be discharged, the auditor's certificate of past profits and the valuers' certificate of the present value of assets.

If the property changed hands during the two years preceding the issue of the prospectus, ascertain the price paid on each transfer as this should enable one to have some idea of the extent to which the cream has already been skimmed and the extent to which the assets are inflated when sold to the company.

5. Vendors' Profits. What is the exact amount of consideration paid to vendors or promoters within the two years prior to the issue of the prospectus? It may be remembered that one of the most elementary forms of company promotion abuses is the giving to promoters and vendors of an unduly large consideration in either cash or shares, so as to leave the company either short of working capital or alternatively burdened with such a heavy capital structure that under ordinary circumstances the shareholders will have no prospect of receiving an adequate return on their investment.

6. Material Contracts. These are contracts with vendors, managing agents, underwriters, etc. In as much as essential information relating to the position and prospects of a company can presumably be obtained by examination of the material contracts into which the company has entered, the law, in order to protect the investor, provides that every prospectus must refer to these contracts. Under the law, however, it is not necessary to set out in the prospectus the gist of these contracts. All that is necessary is to enumerate the parties to them and their dates, with details of the place and time where such contracts may be inspected. The result is that for all practical purposes this protection to investor has proved entirely abortive, for scarcely anyone in practice ever takes the trouble of inspecting these contracts. Most companies, however, do give in the prospectus brief particulars of such contracts as a voluntary measure, and in such cases it is possible for the reader to know something about them.

7. Restrictive Articles. If the articles of the company impose any restrictions upon the members of the company in respect of the right to attend, speak or vote at meetings of the company or of the right to transfer shares, or upon the directors of the company in respect of their powers of management, it is important to study the nature and extent of such restrictions, as they may be very harsh both to shareholders and the directors.

8. Company's Past History. Where the prospectus is issued by an existing company, examine the following information relating to its past history.—

(a) The past results and the present financial position of the company.

The past profits earned and the dividends paid can be ascertained, from the auditor's report included in the prospectus, but with regard to the financial position of the company reference must be made to the recent published balance sheet of the company which is, of course, not given in the prospectus but which must be obtained otherwise.

- (b) The existing share capital of the company *vis-à-vis* the new issue.
- (c) Shares offered, allotted and paid up within the past two years.
- (d) Shares and debentures issued for consideration other than cash within the past two years and the nature of such consideration.
- (e) Particulars of all material contracts made within the past two years.

9. **Names of Bankers, etc.** Note the names of the company's bankers, auditors, legal advisers, and brokers. A knowledge of their standing is sometimes helpful to an investor, because no reputable person would ordinarily lend his name to a prospectus unless he has a reasonable faith in the concern. But at the same time it is important to bear in mind that the names of bankers, auditors, legal advisers and brokers are no guarantee of the soundness of the company issuing the prospectus, because they are not the persons who are going to take any part in the management.

10. **Press Review.** If the prospectus has been advertised in the columns of a reputable financial journal, it will probably be briefly reviewed by the Editor of the paper and his comments should be carefully studied. This may be of considerable assistance to the intending investor. To be on the safe side, it would be wise not to touch the shares of any company which is not recommended by a reliable firm of share brokers or whose prospectus is not advertised in a responsible and discerning newspaper.

In conclusion it may be said that the prospective investor must think twice when tempted to apply for the shares of a new company. He should not give any benefit of doubt to the company when examining its prospectus. With new companies the risk run by the uninformed applicant for shares is enormous. Even if the prospectus be read with the gloomiest cynicism and if most of the glow of the promoters' words be dissipated by the application of a little healthy pessimism, a new venture remains a risk, and should be approached as such. However sound its prospectus may seem on paper, it is liable to accidents. The underwriters may default, or the profit from the company may be squandered, or the concern may be used as the basis for group operations from which none but the manipulators will profit at all.

Statutory Safeguards for Investors

In America the machinery provided by the limited company system has been developed into an engine of fraud, power and oppression; but at the same time the reformist zeal has made far more persistent and heroic efforts to grapple with the evil. The foisting on the public of fraudulent or at least highly undesirable securities of companies has reached in that country, with its elaborately developed art of high-power salesmanship, a far higher degree of perfection than anywhere else in the world. As a natural reaction, preventive legislation has also been carried to a far more advanced degree of stringency. These laws are known as 'Blue Sky Laws.' This is a technical term for the American legislation designed to protect the investor from buying worthless securities, or, as it was picturesquely expressed, from buying so many feet of blue sky,

The investing public in India is also provided with a number of legislative safeguards against the fraudulent activities of company promoters; and these are as follows:—

1. Preventive. Section 93 of the Indian Companies Act prescribes the information relating to promoters, the property to be purchased by the company, the past history of the company, and the like, which must be disclosed in its prospectus, so that an intending investor may find out whether the issue of *shares of debentures put before him is sound or unsound*. Section 98.A makes the rigours of a company prospectus applicable to an offer for sale. Section 277.C prohibits the hawking of shares, debentures and bonds of foreign companies in British India. Finally under the legislation for the control of capital issues, which has been in force since 17th May 1943, no company in British India can issue any capital exceeding Rs. 5 lakhs without the previous sanction of the Central Government. This is an effective safeguard against fraudulent company promotions, since the Government does not give its sanction until it is satisfied that the promoters and their friends are substantially interested in the company.

2. Civil Liability of Promoters. The promoters of companies are subjected to certain civil liability. Section 100 of the Indian Companies Act makes company promoters liable to pay compensation to any investor who suffers loss *on account of any fraudulent statement in a company prospectus*; while section 255 (the most salutary section in the whole Indian Companies Act) makes the promoters of a company, which goes into liquidation, liable to pay compensation for misfeasance.

3. Penal Remedies. Company promoters are also made criminally liable for their fraudulent activities. Under section 337 and 341.A, apart from the ordinary remedy available under the Indian Penal Code against the fraudulent company promoters, the Registrar of Joint Stock Companies is authorised, on a complaint being made by a shareholder, to investigate cases of fraud brought to his notice. After making an inquiry he must report to the Provincial Government, which may order a public prosecution of persons who are believed to be guilty of an offence in relation to the company. Company promoters are also liable, under section 282, to imprisonment if they issue a false prospectus.

Raising of Capital. After a public limited company has been incorporated the first necessity—and one of paramount importance—is to raise the necessary capital. This may be arranged privately or by public subscription; and if the latter course is adopted a prospectus is usually necessary. An appeal for the necessary capital is made to the public by means of the prospectus. Where the capital required is obtained privately from the friends and relatives of the promoters, there is no need of issuing a prospectus; but in that case a statement in lieu of prospectus must be filed with the Registrar.

A company may raise the required finance in several ways, viz—by issuing shares, by issuing debentures or by inviting deposits from the public. When an issue of shares and debentures is offered to the public, it may be underwritten.

The various types of securities issued by companies and the underwriting of securities will be explained in full in a subsequent chapter on the financing of business concerns.

Subscription List. When the prospectus inviting public subscription to the company's capital has been circulated, the next step is to prepare the subscription list. This usually takes the form of separate Application and Allotment Sheets for the different classes of shares, suitably ruled to record the necessary particulars. The prospectus always includes a printed application form, which is filled in by the applicant, and sent, together with the amount payable per share on application to the company's office or to the company's bankers. The subscription list is kept open till the required capital has been subscribed. The list is then closed and the directors proceed to allotment. The term allotment signifies the acceptance by the directors of the offers of the applicants to take shares and the contract is complete as soon as the allotment letter is posted.

Allotment of Shares. A public company cannot allot any shares without complying with the provisions of section 101, which fall under two heads, namely shares (i) where the shares are offered to the public, and (ii) where there is no invitation to the public to subscribe for shares.

When there is Public Offer. No allotment shall be made of any share capital of a company offered to the public for subscription unless the following conditions are satisfied :—

(a) The minimum subscription has been subscribed for. The term minimum subscription means the amount which, in the opinion of the directors, must be raised by the issue of the shares offered to the public for subscription in order to provide the sum, or if any part thereof is to be defrayed in any other manner, the balance of the sum required for (1) the purchase price of any property to be purchased out of the proceeds of the issue, (2) any preliminary expenses and underwriting commission to be paid by the company; (3) the repayment of money borrowed for these purposes, and (4) working capital.

(b) A sum of at least 5 per cent. of the nominal value of shares making up the minimum subscription has been received in cash by the company.

(c) All monies received from applicants for shares shall be deposited and kept in a Scheduled Bank until the certificate to commence business has been obtained by the company under section 103 or the monies so received have been returned to the applicants in accordance with the provision following.

(d) If the minimum subscription has not been obtained within 180 days after the issue of the prospectus, all application money must be returned without interest within the next 10 days. The directors become liable to repay the money with interest at 7 per cent. per annum from the expiration of the 180th day unless they can show that the loss of money was not due to any misconduct or negligence on their part.

When there is no Public Offer. In the case of the first allotment of

shares payable in cash of a company which does not issue any invitation to the public to subscribe for its shares, no allotment shall be made unless the following conditions are satisfied :—

(a) The minimum subscription has been subscribed for. Here the term minimum subscription means either (i) the amount (if any) fixed by the memorandum or articles and named in the statement in lieu of prospectus as the minimum subscription on which the directors may proceed to allotment, or (ii) if no amount is so fixed and named, the whole amount of the share capital other than that issued payable otherwise than in cash.

(b) An amount not less than 5 per cent. of the nominal value of each share payable in cash has been paid and received by the company.

(c) A statement in lieu of prospectus has been filed with the Registrar.

Effect of Irregular Allotment. Section 101 is designed to prevent persons from attempting to float companies with insufficient capital. Any allotment of shares made in contravention of this section is called an irregular allotment. An irregular allotment made by a company to an applicant is voidable at the instance of the applicant within one month after the holding of the statutory meeting and not later or in any case where the company is not required to hold a statutory meeting or where the allotment is made after the holding of the statutory meeting within one month after the date of the allotment and not later.

Return of Allotment. Section 104 requires that every company having a share capital shall, within one month after allotment,—

(a) File with the Registrar a prescribed return of allotment stating the number and nominal amount of shares allotted, the names, addresses and descriptions of the allottees, and the amount paid, treated to be paid or due and payable on each share, and

(b) In case of shares allotted as fully or partly paid up otherwise than in cash, (i) produce to the Registrar for his inspection and examination a contract in writing constituting the title of the allottees to the allotment together with contracts of sale, etc., and also (ii) file with the Registrar verified copies of all such contracts.

Note—Calls on shares, forfeiture of shares, and share certificate are explained in the next chapter.

Commencement of Business. Section 103 provides that a public company cannot commence business or exercise any borrowing powers until it has complied with the following conditions :—

(a) Shares payable in cash have been allotted to an amount not less than the minimum subscription. The term minimum subscription has already been explained above.

(b) Each director has paid to the company on every share taken by him and for which he is liable to pay in cash, an amount equal to the amount payable by the subscribing public on application and allotment.

(c) There has been filed with the Registrar a statutory declaration by the secretary or one of the directors that the aforesaid conditions have been complied with.

(d) In the case of a company which does not issue a prospectus, there has been filed with the Registrar a statement in lieu of prospectus.

On the filing of the statutory declaration, the Registrar will issue to the company a certificate entitling it to commence business. Such a certificate is a conclusive evidence that the company is entitled to commence business. Any contract made by a company before the date at which it is entitled to commence business shall be provisional only and shall not be binding on the company until that date and on that date it shall become binding. It is, however, specially provided that nothing in the above mentioned section is to prevent the simultaneous offer for subscription or allotment of any shares and debentures or the receipt of any application money on debentures.

Test Questions

1. "An industrial label such as 'Joint Stock Company' may bear very different meanings in different circumstances." Distinguish between the important kinds of joint stock companies in this country.

(Bombay B. Com. 1935)

2. There are certain formalities which are to be complied with by a limited company before it is incorporated and also subsequently when it is entitled to commence business. State the same as precisely as you can.

(Agra B. Com. 1916)

3. Describe the successive stages in the flotation of a joint stock company.

(Alld. B. Com. 1936)

4. What restrictions are placed on the choice of a name of a company? Can it change its name and dispense with the use of the word 'Ltd.' as part of its name? If so, subject to what conditions?

(Alld. B. Com. 1938)

5. A company registered in the U. P. decides to shift its registered office to the Bombay Presidency. Is it legally permissible, and, if so, what steps will have to be taken to effect the desired change?

(Agra B. Com. 1917)

6. At what stage of its formation is a company entitled to issue a prospectus? What are the chief facts which the prospectus of a company is required by law to disclose?

(Alld. B. Com. 1937)

7. What information would you expect to find in the prospectus of a company? How would you scan it from the point of view of an investor?

(Alld. B. Com. 1936)

8. What is a prospectus? Critically discuss its contents.

(Bombay B. Com. 1913)

9. Explain the following statements which appear on a company prospectus:—

(a) Consent of the Central Government has been obtained for this issue.

It must, however, be distinctly understood that in giving their

consent the Government of India do not take any responsibility for the financial soundness of any scheme or for the correctness of any of the statements made or opinions expressed with regard to them.

(b) Application will be made in due course to the Committees of the Bombay and Calcutta Stock Exchanges for permission to deal in the shares now being issued. *(Agra B. Com. 1944)*

10. What is the difference between a prospectus and a statement in lieu of prospectus? State by whom and when each one of them is filed.

(Agra B. Com. 1946)

11. What are the statutory requirements to be complied with before the shares and debentures of a foreign company can be offered for sale in British India?

(Agra B. Com. 1945)

Definition. 'It is curious that the law does precisely define the term Director. Section 2 (5) simply states that the term 'director' includes any person occupying the position of a director by whatever name called. Function is everything; name matters nothing.

It is generally accepted, however, that a director is one of those persons who are responsible for directing, governing or controlling the policy or management of a company. Regulation 71 vests the control of a company's affairs in the directors, and, though they may delegate their powers to a certain extent to managers or managing agents, the ultimate responsibility is theirs. A limited company may become a director of another company. Collectively the directors are known as the Board. In some cases, however, they are described as 'Governing Body' or 'Committee of Management'. But by whatever name the managing body may be called, from a legal viewpoint the members composing it occupy the position of a director with all the attendant liabilities and responsibilities.

Number of Directors. Section 83-A provides that every company (other than a private company not being a subsidiary company of a public company) must have at least three directors. It looks, therefore, as though a private company, which is not subsidiary to any public company need not have any directors. But, as Regulation 71 compulsorily provides for the management of all companies (public as well as private) by directors, it is obvious that even private companies must have directors, not necessarily three. If, however, a private company, not being a subsidiary of any public company, does not appoint directors as such but leaves the management of its business in the hands of shareholders, than the shareholders themselves would be deemed to be directors in the eyes of law.

Selection of Directors. As the management of the affairs of a company legally vests in the directors, it is very important that they are wisely selected, so that the company's business may run smoothly and efficiently. Strictly speaking, in the best interests of the company, directors should be chosen for reputation, past experience, technical knowledge, business capacity, financing ability, helping in procuring business or being useful in any other way. Each director should be in a position to make some definite contribution towards the well-being of the company; otherwise whatever remuneration is paid to him would be a sheer waste. In this respect, the directors of a company may be fitly compared to an athletic team, the individual members of which are usually selected on their respective merits, each being expected to make his definite contribution to the winning of the game.

A director is supposed to direct, guide and govern the policy of the company. It is therefore difficult to understand how he can carry on his duties efficiently unless he knows his job properly. If a director is to appreciate readily the various problems that arise from time to time in the administration of a large company, he must possess at least some knowledge of law (particularly company

law), elements of banking and currency, economics, accountancy, finance and psychology ; and he should make himself familiar with the powers and regulations of the company as contained in its memorandum and articles of association. At least one or two directors of the company should thoroughly understand the technical side of the company's business, and one at least should, if possible, be a trained accountant to look after the finances.

All this may sound as a counsel of perfection - not capable of attainment in practice in view of the fact that persons possessing such qualifications are not easily available in this country. That is quite true. In reality, therefore, the selection of directors is governed not solely by the criterion of the above qualifications but by other considerations. Although the law has entrusted the management and control of companies to directors as a body, it is not every director's business to direct. The administration of a large company is an intricate, detailed and whole-time pursuit, which demands a lot of specialised knowledge, and is therefore left to the expert. The board of directors of almost every company is usually composed of two sets of directors—active and passive. The active directors constitute what may appropriately be called an inner cabinet. They are the persons who invariably belong to the managing agents of the company and are nominated by them. It is they who actually control the company's affairs. They spend their life in the business and love it like a child, at least in the case of well-organised and successful companies. They remain more or less permanently in office and are not bound to retire by rotation. They are the men who have had adequate business training and technical experience before their appointment as directors. They naturally resent the interference of other directors who may be termed passive or non-directing directors. But why are such non-directing directors on the board of a company at all, when their real function is not to take any part in the control of the company's affairs? The reasons for adding a few dummy directors to the board of a company may be summed up as follows :—

1. The law requires that every public company and every subsidiary company of a public company must have at least three directors. In order to comply with this requirement, one or two nominal directors may have to be taken in.

2. Sometimes, particularly in the case of new companies, some persons are given a seat on the board for their name and prestige. It may be said that these prestige directors (or guinea-pig directors as they are contemptuously named) are useful in several ways. Their names act first as the bait by which the public is induced to acquire the shares of the company, and, after the company has been financed, as a means of preserving confidence. They also help in consolidating the control which the active director or directors exercise over the company machine. The practice of having, as nominal directors, persons of good position who take little active part in the affairs of a company

is not, of course, in the best interest of the shareholders, as it gives a false sense of security to them and encourages malpractices on the part of the active directors.

3. Some directors get in as the representatives of special interests such as debenture-holders, Government, public bodies, or persons holding large blocks of shares. Such provision is often necessary in order to attract capital.

4. In concerns like banking and insurance companies, where the procurement of adequate business may depend upon the influence of their directors, some directors owe their appointment simply on account of their business connections, as they are expected to bring business to the company. That is why the boards of banks and insurance companies are usually large.

5. Some directors come in merely on account of reciprocity. There are in India a number of well-established managing agency houses, each controlling a number of companies. They select directors for their companies from one another.

It may therefore be said that the composition of the board of directors of a company is based on different considerations. When the Indian Companies (Amendment) Act of 1936 was before the Central Legislature, a number of members wanted that the board of directors of a company should be representative of all interests involved. In opposing this amendment, the Hon'ble Sir Nripendra Sircar very humorously described the working of such a board as follows :—

“Accepting the principle of representation of different interests and the scheme of the Government of India Act democracy, the ideal board composed of different interests will work like this. Mr. Satyamurti will represent one party. Let us have Mr. Rajha on the Board as representing the depressed classes, Mr. Bajoria the Mitakshara Sanatanists and Mr. Joshi the labour. Let us put in Sir Homi Mody on the wholly untenable ground that he has got something to do with business. How will this Board function ?

“Suppose the company is proposing to erect an additional mill and is intending to buy machinery. Sir Homi Mody, a business man, says : ‘We have got plenty of money and money after all makes money. That is my motto. Let us have another mill.’ Mr. Satyamurti will say : ‘Nothing of the kind. Are we going to buy foreign machinery. I won't allow it. We must wait until our nationals produce better machinery.’ Mr. Joshi will have no objection whatsoever to the mill being started provided it is understood that the company will agree to a 20 hour week, double wages and compensation to any worker who runs away without notice. This is how such a Board will function.

“I submit that the directors are in the position of the executive. They are in charge of the management and they must have certain amount of freedom of action, so that there may be continuity of policy. They have to act on the spur of the moment, on the conditions of the money market and so on. It should not be the idea that on the Board you must have representatives of

different interests. In the matter of company management the interests of everybody are to secure a dividend."

Appointment of Directors. With regard to public companies section 83.B (1) provides that, in the absence of any provisions to the contrary in the articles of a company, (i) the subscribers to the memorandum shall be deemed to be the directors until the first directors are appointed; (ii) the directors of the company shall be appointed by the members in general meeting; and (iii) any casual vacancy occurring among the directors may be filled up by the directors, but the person so appointed shall retire at the same time as the person whose place he has taken. Under section 87.1, notwithstanding anything contained in the articles of a company (other than a private company), the directors, if any, appointed by the managing agents shall not exceed in number one-third of the whole number of directors.

It follows, therefore, that if the articles of a public company do not make any provision for the appointment of directors, then the signatories to the memorandum are first directors, and subsequent directors are to be appointed by the company in general meeting. This provision leads to the erroneous belief in the public mind that the appointment of directors is in the hands of the shareholders. But that will be the case only when the articles of the company are silent. In practice the articles invariably contain suitable provisions relating to directors--their number, mode of appointment, remuneration, share qualification, removal, etc., and therefore the provisions of section 83.B (1) are of no practical use at all. According to the usual procedure contained in the articles, the directors of a company are appointed as follows:—

1. The first directors are selected by the promoters (who are to be the managing agents of the company) and are named in the articles. However, according to section 84, a person cannot be named as a director in its prospectus unless before registration of articles or publication of prospectus he has himself or by his agent

- (a) signed and filed with the Registrar a consent in writing to act as such director and
- (b) if a share qualification is necessary, (i) signed the memorandum for his qualification shares or (ii) taken and paid or agreed to pay for his qualification shares or (iii) signed and filed with the Registrar a contract in writing to take and pay for his qualification shares or (iv) made and filed with the Registrar an affidavit to the effect that the qualification shares are registered in his name.

On application for registration of memorandum and articles, the applicant must file with the Registrar a list of persons who have consented to be directors of the company.

2. As stated later on, all the first directors of a company compulsorily go out of office at the first ordinary general meeting. Therefore as regards subsequent appointment, the managing agents have the right to appoint up to one third of

the total number of directors ; then one or two are reserved for appointment by special interests such as Government, States, debenture holders, preference shareholders, municipal or district boards, etc., leaving only a few directors to be appointed by shareholders in general meeting. Thus the shareholders have only a very limited power in regard to the appointment of directors.

Section 83.B (2) lays down that at least two-thirds of the whole number of directors of a public company formed after 15th January 1937 shall be persons whose period of office is liable to determination at any time by retirement of directors in rotation. The ostensible object of this provision was to prescribe that two-thirds of the directors of any company shall retire by rotation and be reappointable only by election by the shareholders. But that is not the case. All that it requires is that two-thirds will retire and will be reappointed by those who appointed them as provided in the articles, which are supreme in this respect. The procedure relating to the retirement of directors by rotation is governed by the compulsory regulation 78.82 of Table A. It is said that the only sound principle of company management is to vest the ultimate control in the directors and to make those directors in turn responsible to the shareholders. This is the purpose underlying these regulations. But, since the re-election of only a few of the total number of directors is in the hands of shareholders, that purpose has not been completely fulfilled.

3. Any casual vacancy occurring among the directors is filled up by the directors without the consent of shareholders, although the director so appointed holds office only up to the time when his predecessor would have retired, if he were subject to retirement by rotation.

4. The chairman of the board of directors as well as of the company is appointed by the managing agents from amongst their own nominees.

~~A~~ **Kinds of Directors.** The directors of a company are known by different designations according to the mode of their appointment. A director appointed by the managing agents is usually called an *ex officio* director. One appointed by debenture-holders is called *debenture director*; and those appointed by other interests are *special directors*. Directors appointed by shareholders are *ordinary directors*. In a life insurance company some directors are appointed by policyholders and are known as *policyholders' directors*, and some are appointed by shareholders known as *members' directors*.

✓ **Share Qualification of Directors.** No share qualification on the part of directors is required by law ; but it is usually fixed by the articles. The extent of their holdings in the company is taken to be an indication of their faith in the company, and the promoter in order to inspire confidence in the investing public frequently arranges for a substantial share qualification to be fixed in the articles. The fixing of a large share qualification is not always in the best interests of the company, as such a procedure has a tendency to attract money rather than brains to the board of directors. It is, however, advisable that the directors should have some stake in the company, no matter how small, since

cannot act as a director ; under section 86-G, a director removed by the company by means of an extraordinary resolution cannot be re-appointed by the directors ; and under section 141-A, a director convicted as the result of an investigation carried out in accordance with section 133 cannot be a director for five years without the leave of the Court.

Position of Directors. Directors are the mere trustees or agents of the company—trustees of the company's money and property and agents in the transactions which they enter into on behalf of the company.

Directors are trustees to the extent that they must exercise their powers as defined in the articles of the company for the benefit of the members generally and not for the benefit of themselves or any particular member. That is to say, they must approve transfers, make calls, issue and allot shares, declare dividends or make investments in the interests of the company as a whole and not in the interests of any particular individual or individuals.

The general law of agency governs to a large extent the relationship between the company and its directors. Directors being in the position of agents for the company are not personally liable on contracts they enter into on behalf of the company provided they do not exceed their authority. If they exceed their authority they will be liable, as are other agents, on the breach of warranty of authority. Thus the directors are special agents and not general agents, that is to say, they have no authority to act in all matters concerning the company, but only have such powers as are definitely given to them by the company's memorandum and articles. Directors like other agents are entitled to be indemnified by the company against all losses and expenses properly incurred by them in the due performance of their office.

Powers and Duties of Directors. The compulsory regulation 71 of Table A lays down that the business of a company shall be managed by its directors. This regulation expressly delegates to the directors the power to do everything that the company can do *except* where the authority of a general meeting of the company is expressly prescribed by the Act and the articles of the company. Some of the principal powers of directors consist of allotment of shares, making calls, forfeiture of shares, rectification of the Register of Members, rejection or approval of transfers, making contracts, incurring capital expenditure and recommendation of dividends. "*Delegates non protest delegare*"—a delegate cannot delegate his authority. The directors cannot therefore delegate their powers unless the articles of the company expressly provide for such delegation, e. g., regulation 91 of Table A.

A company is an entity distinct alike from its members and directors. Some of its powers may, according to its articles, be exercised by directors, while certain other powers may be reserved for the members in general meeting. Where the powers of management are vested in the directors, as they are by regulation 71 of Table A, they and they alone can exercise those powers. The shareholders cannot usurp the powers which are vested in the directors any

likely to find any great difficulty over this section, for if it is to the interest of the company that a managing agent should act also as a selling agent for the company, it will always be possible to secure the shareholders' consent to the arrangement.

Section 86-F. Under this section, without the consent of the directors, a director of the company, of the firm of which he is a partner or any other partner of such firm, or the private company of which he is a member or director, can not enter into any trading contract with the company. It is against all canons of morality to encourage practices involving an inevitable conflict between duty and interest. A director holds a fiduciary position and to allow him to deal with a company on his own account and for his own benefit seems to be reprehensible. Of course, under section 91.A, an interested director is required to disclose his interest at the meeting of directors, and under section 91.B he cannot vote on the contract in which he is interested, nor is he included in the quorum. Further, under section 21.A, a company must keep a register for recording particulars of all contracts in which the directors are interested, and this register is open for the shareholders' inspection.

These safeguards not necessarily protect the company fully. There is nothing in sections 91.A and 91.B to assure the shareholders that the provisions of these sections have been duly complied with. The minutes of board meetings alone can show whether they have been complied with, but these minutes are not open to shareholders' inspection. Moreover the sections in question are not always effective as the directors do not always watch the interests of shareholders as against those of the interested director. In practice it may be that the directors accommodate each other.

Section 86-G. This section provides that a company may by an extraordinary resolution remove any director whose period of office is liable to determination at any time by retirement of directors in rotation before the expiration of his period of office and may by an ordinary resolution appoint another person in his stead. If a director should be removed in this way, he may not be re-appointed by the board of directors.

Section 86-H. Under this section, the directors of a public company or of a subsidiary company of a public company cannot, without the consent of the company concerned in general meeting, sell or dispose of the undertaking of the company or remit any debt due by a director.

Section 86-I. The office of a director is vacated if he (a) fails to obtain the qualification shares within the time fixed or at any time thereafter ceases to hold them; (b) becomes of unsound mind or is adjudged insolvent; (c) fails to pay off calls within six months from the date of the calls; (d) contravenes the provisions of sections 86-D, 86-E, or 86-F; (e) absents himself from three consecutive meetings of directors or from all meetings of directors for a continuous period of three months (whichever is the longer) without leave of absence from the board of directors; or (f) contravenes any other prohibition prescribed by the articles.

How do Directors act ? The directors of a company usually direct the affairs of a company by decisions of the majority. But in some cases the law requires a statutory majority of the directors. Thus the managing agents of a company cannot enter into any trading contracts with it without the consent of three-fourths of the directors present at a board meeting and entitled to vote on the resolution ; or the managing agents of a company cannot invest the funds of one company in the shares and debentures of another company under their management unless the purchase has been previously approved by a unanimous decision of the board of directors of the purchasing company. These requirements of law take away the joint responsibility of directors.

Vacation of Office. The directors of a company vacate their office in accordance with the provisions of section 86.F as described above, or, if they are removed by an extraordinary resolution of the company according to section 86.G. Subject to articles, a director may resign his office at any time and the power to accept such resignation is usually given to directors. A director may also be removed under the common law by shareholders on account of pecuniary misconduct, negligence, incompetence or permanent disability.

Liability of Directors. The directors of a company may incur liability in various ways. In the first place, they may become liable to pay damages (a) to outsiders for contracts when they exceed their authority or when they contract in their own name, for torts (i. e., wrongdoing such as the infringement of a patent), or for untrue statements in the prospectus ; and (b) to the company for negligence as agent or for misfeasance or breach of trust, e. g., breach of articles resulting in loss to the company, application of the company's funds to *ultra vires* purposes, secret commissions and bribes, improper payments, etc.

The directors are liable for negligence or breach of trust in relation to the affairs of the company. While the company is a going concern, the remedy is by an action at law, but after liquidation has commenced proceedings may be taken under section 235. If it appears in the course of winding up that there has been misfeasance or breach of trust, the Court may on the application of liquidator or any creditor or contributory examine into the conduct of such person and compel him to pay damages. Misfeasance is a breach of duty not involving the misapplication of the company's funds, but resulting in a loss to the company. Breach of trust is a misapplication of the company's funds. A director who has been rendered liable is, however, entitled to contribution from his co-directors equally liable.

Secondly, in certain circumstances the directors may become criminally liable. Under section 236 they are liable to fine and imprisonment for destruction or falsification of books, accounts, etc. Under section 237 they are liable to prosecution by the Court during the winding up of a company if they are guilty of a criminal offence. Under section 282, they are liable to fine and imprisonment for wilfully making false statements in any accounts, reports, certificates, etc.

Thirdly, the directors may also become liable to fine if they do not comply with certain provisions of law.

Managing Agents

In India, unlike in other countries, the management of limited companies is mostly in the hands of managing agents. A characteristic feature of organised industry and commerce in all the chief Indian centres is the presence of the large agency firms. In addition to participating in the import and export trade, they finance and manage industrial ventures all over the country and often have several branches in the large towns.

This system is the outcome of conditions which are peculiar to India. It has so to speak grown up with India's industrial development. It is customary to adopt the view that the managing agency system is peculiar to India and is not found anywhere else in the world. It is found to a small extent in Great Britain also. That the system which is almost universal in India is uncommon in Great Britain is undoubtedly a fact, due to the different circumstances under which industry has developed in the two countries. But that it is non-existent in other countries is incorrect. The term itself is infrequently used but the system exists nevertheless and for the same reason as the original managing agency houses came into being in India. The firms exercising this function in Great Britain are normally classified as managers or secretaries. They hold their position normally by their expert knowledge of a particular line of business and do not as a rule manage the same variety of companies as the managing agency houses in India. The most noticeable industry in which the practice is firmly established is that of shipping. There are a score of companies, some of them famous shipping lines, which are under the management of firms of managing agents. It is noteworthy that one of the lines, the Motor Lines, Ltd., has as its general managers and secretaries, Walter Runciman & Co., Ltd., a name famous both in shipping and politics. This form of management is not, of course, confined to the shipping industry alone. An important parallel is provided by the Kolar Group of Gold Mines. Messrs. John Taylor & Sons, the well-known mining experts, are managers of this Group. In the case of numerous tea companies quoted on the London Stock Exchange, the companies are managed by managing agents, agents and secretaries, or secretaries, working under the boards of directors. A procedure closely analogous to managing agency system is found in Britain in connection with the management of many of the well-known investment trust companies both in England and Scotland. A number of these companies are managed by firms of managers or managers and secretaries, who each control a number of companies in a manner very similar to the Indian. It is not unusual for from five to eight companies to be managed in this way by one firm of managers. *Capital*, 19th July 1936.

Origin of the System. To form a clear idea of the part the system of managing agents has played in Indian industrial development it is necessary to trace its origin and see the lines along which it has developed. The early

pioneers of industry in India were British merchants who first came out to India as representatives of some trading companies. They were men who were first engaged in the general trading business, but soon turned their attention to other lines of activity. They found themselves in a large agricultural country, rich in natural resources and with a vast consuming population and a plentiful labour supply but industrially quite undeveloped. Public confidence was lacking, however, and there was no large class of people willing to let others have the use of their money for the purpose of investing in the industry.

In consequence, the early pioneers of industry found their enterprises severely limited by the resources which they could put up themselves or persuade their friends to provide. They started industries, formed partnerships and advanced the capital for starting and carrying on their business. Often they had to nurse industries through many years of loss, for it was only after a concern had become visibly successful that there could be any hope of attracting investors from the outside public. When, however, this stage was reached and the major elements of risk seemed to have been eliminated, it was possible for a business to be turned into a public company, and the successful pioneers were able to get back a considerable part of their capital by selling a large portion of their business. Having thus released their capital they were ready to enter into fresh enterprises. As part of the process of starting the public companies, the founders became managing agents to the companies and secured a long term of management by virtue of agreements between themselves and the companies. Thus in parting with their interests, they were careful to retain their power of control over the businesses they had founded. Another reason for the growth of the managing agency system was the difficulty of finding suitable managing directors who could remain in the country for a sufficiently long time to guarantee the continuous management of the concerns entrusted to them.

Thus the managing agency system grew up in Bengal on account of the special economic conditions in which the British merchants found themselves. More or less the same circumstances led to the establishment of the managing agency system in Western India. There the Indian merchants who were engaged in general trade and more particularly in the cotton trade began to take interest in the development of industry. In this direction they received considerable help from the resident English representatives of British machinery manufacturing firms. They also had the same difficulties as the British merchants in Bengal, namely, there were no industrial leaders and no large investing class in the country.

A further factor which led to the managing agency system in India was the company law. Till 1913 it was not compulsory for companies to have any directors at all. It was therefore possible to devise a system by which the persons interested in companies made themselves managing agents. When the Indian Companies Act of 1913 made the appointment of directors compulsory in the case of public companies, the managing agents had no difficulty in getting

in India. Not every managing agent can claim the ability, prudence, or resources of the great business houses by whom the system was founded, but every agent, whatever his capacity for fulfilling the functions of managing agents, benefits by the tradition and to a large extent owes his existence to it.

Constitution of Managing Agency Firms. According to law the managing agency of a company may be in the hands of a person, firm or company. But managing agencies are chiefly in the form of partnerships or private limited companies. In some cases, particularly in Ahmedabad, public limited companies also act as managing agents. The managing agency houses are either European or Indian.

The European agency houses are usually constituted on the basis of heredity and selection. The original founder of the agency firm has his family represented on the firm by one or more members, and selected outsiders are also taken into partnership from time to time. These outsiders bring with them not only capital and industrial experience but also some technical knowledge. The Indian agency houses are, however, conducted more or less as family concerns, and no outsiders are usually admitted into partnership. It does not mean, of course, that the succession to a firm by the son or heir of the family is necessarily a mistake; but when this occurs to the exclusion of other talents and experiences, the results are unsatisfactory.

Dominance of Managing Agents. Efficiency of company managements depends largely upon the extent to which its executive consisting of directors and managing agents enjoy freedom of action without being hampered by excessive interference by shareholders. In this respect the managing agents in India have been at a great advantage compared with company executives in other countries. The managing agency system is in almost all cases a form of economic oligarchy. The managing agents secure complete control over the companies under their management in some or all of the following ways:—

1. They secure control by means of written agreements with their companies. Under section 2 (9A), a managing agent is defined as a person, firm or company entitled to the management of the whole affairs of a company by virtue of an agreement with the company and under the control and direction of the directors, except to the extent, if any, otherwise provided for in the agreement. It means that, by an agreement with the company, it is possible for managing agents to be independent of the control and direction of the directors in such matters as may be specified in the agreement.

2. They usually retain a substantial block of shares in the companies under their management; and the shares are commonly those which carry large voting rights. It is not possible to find out in each case the actual extent of their holdings, as the shares are held in the names of various persons who are directly or indirectly allied to the managing agents.

3. In some cases, they are the principal debenture-holders and creditors of companies. The dependence of companies on the finance supplied by manag-

ing agents naturally tightens up the grip of the latter over the former. Section 87.A (2) provides that the managing agents of all companies formed before 17th January 1937 will not continue to hold office after the expiry of twenty years from that date. But the termination of their office will not be effective until all monies payable to them have been paid.

1. The shareholders of companies are sometimes many and are scattered over long distances. They do not know one another, and their individual stake in the company is often very small. Under such circumstances they cannot be expected to come together and operate against the managing agents.

5. The directors, who are supposed to supervise the managing agents, are not in many cases in a position to do so, because most of them owe their appointment either directly to the managing agents themselves or indirectly to their influence. Then there are some directors who hold so many directorships that they are simply indifferent and unable to perform their proper function.

Advantages of Managing Agency System. The managing agency system, a unique feature of our industrial organisation has been subjected to unfair criticism from time to time. But is the system really so bad as it is sometimes made out to be? Let us therefore see what are its advantages or what services it continues to perform to our industries and commerce.

✓ 1. *Promotion* It is a well-known fact that before any industrial concern can be started, a certain amount of preliminary work has to be done; and this requires the expenditure of both money, and technical and financial talent. There are no company promoting agencies here just as there are in Western countries. Under such circumstances, some one individual or a group of individuals must take the initial risk of investigating into the possibilities of the successful working of a new concern and start preliminary operations. All this work is done by managing agents. In the West the promoters are rewarded for their services by a cash payment or by the free allotment of a certain number of the company's shares. In India the managing agents who act as the promoters are entrusted with the management of companies which they take the trouble of creating.

✓ When a company is formed to purchase some existing property the managing agents either buy or buy the right to buy such property before the company is actually incorporated and the more responsible managing houses in India usually pass on such properties to the companies at cost price, whereas in other parts of the world company promoters usually transfer such properties to companies at inflated values and thus take flotation profit.

✓ 2. *Underwriting.* In order to secure from the public the capital required by a company, it is often necessary that there should be some trusted intermediary to bring together the moneyed investing public and the needy but brilliant company promoter. This function is performed in England by underwriting or issue houses, in Germany by industrial banks and in U. S. A. by

investment banks. ✓ There are no such institutions in India. ✓ Here all these services are rendered to companies by their managing agents. They act as underwriters and assist in the placing of shares on the market and the mobilisation of the people's savings for industrial purposes.

✓ 3. *Finance.* The managing agents render an essential service to industry by providing finance for the starting of new companies or the expansion of existing ones. It is noticeable that, even in centres where joint stock companies are fully established and their principles understood, it is rather difficult to start a new venture, unless the promoters have, at their private disposal, a considerable proportion of the requisite capital resources. It is true that in recent years when money in the hands of the public has been plentiful, numerous companies have been formed in India almost entirely with public money; but since the control of capital issues came into force on 17th May 1943 the Central Government before granting permission for the raising of capital from the public ordinarily requires that the promoters themselves should furnish a substantial portion of the capital.

✓ In many cases it is only when a business becomes demonstrably profitable, that it can with confidence be thrown open to public subscription. Until then the promoters must be prepared to provide the capital requirements from their own resources. ✓

Some companies raise a part of their capital in the form of deposits received from the public. Here again the managing agents form a necessary link in securing such finance. The readiness of the public to deposit their funds and the rate at which they lend the money depend entirely upon the credit and financial standing of the managing agents of the companies concerned.

✓ Moreover, the banks in India are generally reluctant to advance money to limited liability companies unless the managing agents are prepared to furnish personal security. There have been instances in which the managing agents have undertaken very considerable risks in the way of personal liability in order to save the companies under their management.

In circumstances such as these, the anxiety of managing agents to occupy a dominating position of control with respect to their companies is understandable. The freedom from control by the shareholders, which such a position ensures to managing agents, has been severely criticised; but, while it admittedly leads to abuse in some cases, the fact is that in the hands of efficient and honest managing agents, who are able to pursue their policy without undue interference, it can prove of great benefit to the companies controlled. *

4. *Rationalisation.* Apart from providing the promoting and financing services, the managing agency system often leads to more efficient and economical management of companies than would otherwise be possible.

A big firm of managing agents controls, for example, a number of companies owning tea estates, jute mills, collieries, etc. For the efficient management of these various concerns, the firm will have separate departments orga-

nised on the lines of each industry—a tea department, a jute department, a coal department, a shipping and insurance department, etc.—thus ensuring that the companies controlled by them engaged in the various industries receive the special attention which they require. It will have in addition its own purchasing and sales organisation dealing with the purchases and sales of all the companies under its control.

The advantages of managing agency of this nature to the companies concerned are obvious. In the first place, they obtain at a comparatively reasonable cost the services of men of outstanding ability and long business experience, who normally constitute a big and important managing agency firm. Services of men so highly qualified would be beyond the reach of the companies if they had to find them for themselves.

In the second place, the system ensures a further economy to the companies. When a jute mill, a coal company, a tea garden and a transport company are under the same management, the products of one concern find a market, or at least a small outlet, in the business of the others. Thus a transport company is assured of a certain amount of business, because the goods of all the allied concerns will doubtless be sent through it. Similarly a coal company is sure of finding an outlet for its product in the allied jute concern or tea factory. Those concerns which need packing material may be expected to utilise the products of the jute company under the same managing agents.

In the third place, they get the advantage of having at their disposal highly qualified technical and supervisory staff whom they could not ordinarily afford to employ themselves.

Finally, the managing agents, with their purchasing and sales organisation, are able both to buy and to sell to the best advantage of the companies. An organisation buying in bulk, in constant touch with and possessing an intimate knowledge of the market, should be obviously in a stronger position than an individual buyer, while a firm selling, say, for a dozen jute mills should obtain better results than a dozen persons of various degrees of competence, each selling for one mill.

— In this way, companies under a big firm of managing agents secure, without an actual combination, all the advantages of rationalisation in the matter of buying, manufacturing, selling, marketing, propaganda, research and finance. —

5. *Safeguard for Investors.* The managing agency system is indeed a great safeguard for the investing public, since they know that the big agency houses value their reputation far too highly to risk failures and are prepared to make substantial sacrifices to protect their good name. The managing agents are often of real service to companies in temporary difficulties. Thus, when the tea and the cotton industries were passing through a period of depression and banks were unwilling to advance money to them on account of the losses which

they had suffered and their very existence was threatened, it was the managing agents who came to the rescue of the companies under their care, and, by furnishing the requisite finance, enabled them to weather the storm. There have been numerous instances where the managing agents have written off considerable losses to themselves in order to help through difficult times companies that had a prospect of ultimately making good and benefiting the community as a whole.

In addition to the specific services rendered in saving the weaklings from collapse in times of difficulties, managing agents create a feeling of confidence and trust when it is most needed. The managing agency system has contributed more than any other single measure or method to remove the distrust and insecurity which has prevented Indian capital from participation in industrial ventures. Indianisation of the share capital of companies has gone on rapidly. What stimulant did attract Indian money out of its shy hoards? For a regular flow of capital into profitable and productive channels two conditions are essential—a steady stream of income and the growth of trust and confidence in the men who control and manage business. Indian-owned capital admittedly began to participate in industrial ventures at the beginning of this century. Excepting at intervals, which have been caused by general world conditions, the process has continued and India today is meeting an increasingly large proportion of her capital requirements internally. And this fact certainly indicates an increasing amount of faith and confidence in the men who have been instrumental in bringing about this state of affairs. In India, in Bengal particularly, the confidence of the public has been established, and there can be no hesitation in attributing it to the steady and conservative control of industry by managing agents, who saw profit to their name in profits honestly earned, and so built up a reputation for integrity and sound business sense.

✓It is commonly conceded in the financial circles of Calcutta that a venture promoted under the auspices of a firm of managing agents stands a better chance of attracting public money than does a company with an independent and wholesome executive. ✓This is largely because the managing agents affix to the prospectus of the company the seal of their approval and give the new concern a promise of steady and sound control. The investor's risks are accordingly minimised and the hallmark of a reputable firm is often sufficient inducement to him for investment. In the absence of special institutions, which could furnish sound advice to investors in the matter of their investments, it is a good thing that old and trusted firms should sponsor new industrial ventures and afford protection to investors.

Defects of Managing Agency System. As already stated, managing agents secure effective control of the industrial concerns they manage. The wide powers possessed by the managing agents can obviously be used either primarily for the good of the joint stock companies or for the good of the managing agents themselves; and, human nature being what it is, it is hardly likely that the

system should have reached its present degree of development without complaints that the less altruistic policy is sometimes adopted. The system has, therefore, brought in its train a number of serious abuses.

1. *Financial Dominance.* Under the managing agency system, industry tends to be dominated by financial rather than industrial considerations. The managing agents are people who can supply the necessary finance, rather than people who have the necessary technical knowledge to carry on the industry. Hence, if a company gets into difficulties, the managing agents are more likely to assign their rights (of course, with the consent of shareholders) to another firm that is financially stronger than to a firm technically better qualified to carry on a particular business.

2. *Excessive Speculation in Shares.* The managing agency system has been occasionally responsible, particularly in Bombay, for the excessive speculation in shares of companies. Any weakness in the financial position of the managing agents, quite apart from the position of any particular company which they control, once it becomes known or suspected, leads to speculative activity in the share market on the part of those who wish to get control of the company by acquisition of a majority of shares. Such weakness of the managing agents immediately reacts on the position of the companies which they control, though these may themselves be quite sound. Many of the crashes which have disgraced the Bombay Stock Exchange from time to time have been the result of the interdependence between the managing agents' external activities and their functions as financial agents of the companies in their charge.

3. *Laxity of Directorial Control.* Companies' boards of directors are often unduly weighted with nominees of the managing agents, and care is taken to provide in the articles of the companies in such a way as to prevent this weightage being disturbed by any move on the part of shareholders. Instances are not wanting where directors under the control of managing agents have issued deferred shares with multiple voting rights (which have been bought up by the managing agents) not in the interests of the company but in order to enable the managing agents to retain control. The directors of joint stock companies in this country usually lack the idea of responsibility which their position entails. They consider their occupation to be more or less formal and take it for granted that everything would be looked after by the managing agents who are virtually their masters. The extraordinary powers conferred upon the managing agents have turned them from managers into masters, and the supervision of the directors has become a farce. ✓

Moreover, a large number of directorships are frequently held by a single individual, who in one way or another is connected with the managing agents. This practice has tended to concentrate the directorships in the hands of a very limited number of men. The result is that their attention to their duties is irregular and inefficient. Many of them look upon their job as a mere sinecure for the purpose of making some extra income.

4. *Inter-investment.* In many cases there has been the objectionable practice of inter-investment of funds among concerns under the same management. Of course, loans between two or more companies under the same managing agents are now prohibited by law; but the purchases by one such company of the shares and debentures of another are still permissible with the unanimous consent of the directors of the purchasing company. Such a method of financing is highly questionable. There may be no evil consequences when the financial standing of both the companies is very good, but the interests of the shareholders are adversely affected when the funds of a strong company are employed in financing a comparatively weaker concern. The debentures issued by one company may be subscribed entirely or mainly by other companies under the same management. This interlocking of interests often spells ruin even for financially sound concerns which have been tacked on to weaker ones. It also tends to perpetuate quite wastefully the life of even thoroughly insolvent or unsound concerns which in the larger interests of the community as a whole should be immediately closed down. This artificial propping up of weak companies is often due to the managing agents' desire to retain their remunerative job.

5. *Incompetent management.* The managing agency agreements are entered into for a fairly long period, now, of course, limited to twenty years; and managing agency firms, particularly Indian, are constituted as if they were family concerns, even though the son however incompetent succeeding his father. The hereditary principle is economically unsound, for there is the danger of the firm falling into incompetent hands, as in practice it often does. It therefore leads to incompetent management. Very often it happens that even after the able and energetic proprietors of a firm of managing agents, with whom the management contract had been originally made, have retired or passed away, the management has still to be continued with their successors in the firm even if they are found to be absolutely incompetent or indifferent; and this is highly detrimental to the interests of the shareholders concerned.

6. *Exploitation.* Companies are frequently exploited by their managing agents in one or more of the following ways:—

(a) *Misuse of Inside Information.* The managing agents, with their inside knowledge of the working of the companies which they manage, are able to manipulate their share holdings in the various companies in such a way as to ensure the maximum profit for themselves, irrespective of the interests of the shareholders. They may declare dividends to suit their own interests; they may depress or inflate the price of shares by declaring low or high dividends to serve their own purpose and to speculate at the expense of the shareholders and the public, even when such declaration of dividends is absolutely unjustified by the results of the working of the company.

For instance, in the case of a certain jute mill company, although this company was making very large profits and all the other jute mills were paying

money for their private purposes. Although public companies and their private subsidiaries are not now allowed to make loans to or to give guarantees in favour of managing agents, yet managing agents may still maintain a current account with the company for purposes of the company's business. Strictly speaking, a credit held by managing agents in a current account with their company is another form of a loan which they may partly use for their own purposes.

(f) *Unnecessary Capital Expenditure.* The managing agents very often extend the operations of companies out of profits instead of distributing them in dividends. They add buildings, purchase new machinery even when the existing machinery cannot be profitably employed full time, provide for various other extensions on the plea of improvements even when the probable results do not justify the expenditure involved. All this they do for the simple purpose of keeping as much property under their control as possible and also for the purpose of earning additional commission on capital expenditure where they are entitled to do so.

(g) *Waste of Funds.* The managing agents and their favourite directors, who are often in league with one another squander away the resources of companies in various ways, and in particular by employing officers at disproportionately high salaries. These officers who are usually connected with the managing agents make in one way or another large illegitimate income out of the funds of companies.

Statutory Control of Managing Agents. The managing agency system has been prevalent in this country for a very long time; but no provisions existed in the Indian Companies Act of 1913 to deal with the special position of managing agents. The developments, however, that had taken place in joint stock company management since 1913 made it imperative that the managing agency system should receive recognition and that any amendment of the Companies Act should contain provisions for the control of managing agents. Such provisions were therefore introduced in the existing company law by the Indian Companies (Amendment) Act of 1936. By that time the position had been reached when a decision had to be made whether the system, in its own interest as well as in that of the public, should or should not be subjected to certain legal restrictions. On the one hand, it was argued that to impose restrictions on a system which had been instrumental in building up Indian industries must endanger the further development of those industries; while on the other hand it was urged that the abuses to which it had led were themselves the principal hindrances to further industrial development. It was also contended that no amendment of the Companies Act, however stringent, can make company scandals impossible. They occur in every country of the world and under every system of management, for no statute can make all men honest. The best safeguard for the shareholder is increasing education of the investor in the art of discriminating between good and bad managements. If he hazards his investment in the pursuit of good dividends, that is his affair and he must not complain if occasionally he fails. Occasional failure and the elimination of the unfit is the justification of the

capitalist system. But this kind of argument did not find favour with the Indian legislature and the managing agency system was brought under statutory control.

The amendments made in 1936 in the Indian Companies Act of 1913 aim, in the first instance, at the greater education and enlightenment of the shareholders and the public in the affairs of joint stock companies. Thus provision has been made rendering compulsory the disclosure, in the prospectus, of the terms of managing agency agreements and of the names of partners of managing agency firms, together with the nature of the interest, direct or indirect, of the directors of companies in the managing agency firms. The keeping of appropriate books and the publication of more details in balance sheets and profits and loss accounts are prescribed, and the Government has taken power to require explanations and make inquiries, and, in extreme cases, to institute criminal proceedings if a company appears to be guilty of fraudulent trading.

The legal provisions are intended to correct the specific abuses of the managing agency system; and how and to what extent they do so are described in the following paragraphs.

1. *Appointment.* Under section 87.B(f) the appointment of the managing agent is not to be valid without the sanction of the company in general meeting, but the appointment made prior to the issue of the prospectus statement in lieu of prospectus is exempt from such sanction. This exemption renders the power of shareholders illusory and ineffective. As a rule, the managing agency agreement is made prior to the issue of the prospectus and the mischief arises out of such arrangement, although it is invariably mentioned in the prospectus itself, because individual shareholders seldom care to acquaint themselves with the details given in the prospectus. It is, however, argued that, if the terms upon which the managing agents are to act are set out in the prospectus and the public subscribe upon that basis, it would be most unfair if at the statutory or other general meeting of the company, the members refuse to sanction the appointment of the managing agents or endeavour to alter the proposed managing agency terms. If any one does not approve of the managing agents or the remuneration to be given to them, he need not apply for shares.

It is interesting to know how the first managing agents of a new company are actually appointed. The first set of directors who are practically friends and nominees of the promoters (who in their turn become the managing agents) appoint the first managing agents on the managing agency terms set out in the articles. Under powers delegated to the directors by the articles, the directors sign the agreement between the managing agency firm and the company, so that in practice the appointment of the first managing agents does not come up before the shareholders at all.

Section 86.A provides that if an undischarged insolvent acts as a managing agent of a company, he is liable to imprisonment and a heavy fine.

2. *Duration.* By section 87.A public companies and their private subsidiaries are prohibited from appointing managing agents to hold office for more than twenty years at a time, and all managing agencies existing on 15th

January 1937 will automatically terminate within twenty years after that date. At the end of the period it will be open to the company in general meeting to renew the agreement for a further period of twenty years, and if the agreement is not renewed, the managing agent of the company will be entitled to a charge upon the assets of the company by way of indemnity for all liabilities or obligations properly incurred by him on behalf of the company subject to existing charges and encumbrances, if any. Moreover, all monies payable to the managing agents for loans made to or remuneration due from the company must be paid before the termination of the managing agents' office can take place.

This provision is based on the sanctity of social justice and public good and does not regard any contract—much less an unconscionable arrangement—as sacrosanct. There is, however, no suitable safeguard to prevent existing agents devising subtle means for defeating these provisions of law by enlarging the business of the company or starting new lines or raising fresh capital, thus keeping the companies indebted to them so that they may continue in office.

3. *Remuneration.* Section 87.C provides that after 15th January 1937 when any company appoints or reappoints a managing agent, his remuneration must be based on a fixed percentage of the net annual profits calculated after allowing for interest on loans and depreciation but before any deduction in respect of income-tax or interest on debentures. If the managing agent's remuneration is to be calculated on any other basis, a special resolution of the company is required. The managing agency agreement can, however, provide for a minimum payment in the case of absence or inadequacy of profits together with an office allowance. But no maximum has been laid down for determining the minimum sum to be paid in the absence of profits or as office allowance.

4. *Powers.* According to the statutory definition of the term 'managing agent,' given in section 2 (9A), the managing agents, by virtue of an agreement with the company, are entitled to the management of the whole of its affairs; and they can be independent of the control and direction of directors in such matters as may be specified in the agreement. But under section 87.G directors are prohibited from delegating to managing agents the power to issue debentures; and under the same section the managing agents cannot invest the funds of the company without the consent of the directors. Except in the matter of issuing debentures and making investments, the managing agents' authority has not been restricted.

5. *Removal.* The managing agents, once appointed for a fixed term, cannot be removed by the shareholders unless provision for their removal is made in the articles and the agency agreement. But section 87.B (a) provides that a company may remove a managing agent by a simple resolution passed at a general meeting if he is convicted of an offence in relation to the affairs of the company punishable under the Indian Penal Code and being under the provisions of the Code of Criminal Procedure non-bailable. The managing

public policy that he should deal with the company on his own account and for his own benefit.

11. *Inter-company Investments.* Section 87.E provides that no public company can loan its money to any other public company under the management of the same managing agent. Closely allied with the question of inter-company loan is the question of the acquisition by one company of shares and debentures of another company under the management of the same managing agent. By section 87.F such investments require the unanimous decision of the board of directors of the purchasing company.

12. *Competing Business.* Section 87.H provides that a managing agent shall not on his own account engage in any business which is of the same nature as directly competes with the business carried on by a company under his management or by a subsidiary company of such company.

13. *Managing Agents' Directors.* Section 87.I provides that the number of directors of a public company appointed by the managing agent shall not exceed one-third of the whole number of directors, notwithstanding anything contained in the articles of the company.

14. *Contracting out.* Section 86.C prohibits a managing agent of any company from contracting out of his legal responsibilities.

The managing agents are also made responsible for the proper maintenance of the companies' books of account. They are bound to render all possible assistance to liquidators on pain of imprisonment and fine.

In conclusion it may be stated that the managing agency system rendered valuable services to Indian industries in the past. It has been in force in India for over three quarters of a century and without its help the industrial development of the country would never have reached its present stage. Perhaps the finest thing that can be said of it is that no one invented it. It has just grown with the years and the requirements of India, constantly moulding and adapting itself to the changing scene. The best testimony to its efficacy is to be found in the fact that while it is indisputably British in origin Indian business men are in increasing measure exploring its possibilities and building up indigenous managing agency houses which are daily growing in stature and repute.

Those who advocate the abolition of the managing agency system do not realise the fact that, even if the system is done away with, the persons now connected with the various agency houses will continue in one form or another to represent the best industrial ability and experience available in the country, and, whatever be the form of company management, they will undoubtedly remain the captains of industry. Moreover, free India is now on the threshold of big industrial development and urgently needs the services of agency houses of ripe experience and great financial resources. Managing Agents perform a wide variety of functions which cannot all be undertaken by ordinary boards of directors. The managing agency system is still needed where considerable pioneering work is involved in the establishment of a new industry and where

exercise supervision over its affairs. Let us therefore see what statutory power the shareholders of companies in India possess in this respect.

(a) Directors.

Appointment. With regard to public companies, section 83.B (1) provides that, in the absence of any provisions in the articles of a company, (i) the subscribers to the memorandum shall be deemed to be the first directors until the first directors are appointed; (ii) the directors of the company shall be appointed by the members in general meeting; and (iii) any casual vacancy occurring among the directors may be filled up by the directors, but the person so appointed shall retire at the same time as the person whose place he has taken. Under section 87.1, notwithstanding anything contained in the articles of a company other than a private company, the directors, if any, appointed by the managing agents shall not exceed in number one-third of the whole number of directors.

It follows, therefore, that if the articles of a company do not make any provision for the appointment of directors, the directors can be appointed only by members in general meeting; and this leads to the erroneous belief that the members of a company control the appointment of directors. But that is not the practice. The articles of all companies do make the necessary provision for the appointment of directors. They fix the total number of directors to be appointed and prescribe the mode of their appointment. One third of the total number of directors is in the first instance allotted to the managing agents; then one, two or more are reserved for appointment by special interests such as debenture holders, preference shareholders, Government, States, Municipal or District Boards, etc., leaving only a small fraction of the total to be appointed by shareholders in general meeting. Thus the shareholders have only a very limited power in regard to the appointment of directors.

Section 83.B (2) lays down that at least two-thirds of the whole number of directors of a public company formed after 15th January 1937 shall be persons whose period of office is liable to determination at any time by retirement of directors in rotation. The ostensible object of this provision was to prescribe that two-thirds of the directors of any company shall retire by rotation and be reappointable only by the election by the shareholders. All that it requires is however, that two-thirds will retire and will be re-elected by those who appointed them as provided in the articles, which are supreme in this respect. It will thus be seen that this provision does not help the shareholders very much.

Removal. Under section 86.G, the members of a company may by extraordinary resolution remove any director, whose period of office is liable to determination at any time by retirement of directors by rotation, before the expiry of his period of office and may by ordinary resolution appoint another person in his stead. The person so appointed shall retire at the same time as the person whose place he has taken.

Under common law the members of a company have also the right to

ing how its affairs are being conducted. These reports and accounts are considered by shareholders in general meetings and approved by them. The necessary meetings held for this purpose are as follows :—

(a) *Statutory Meeting.* In the case of every public company limited by shares or limited by guarantee and having a share capital, a general meeting of the members must be held not earlier than one month and not later than six months from the date on which the company is entitled to commence business ; and not less than 21 days before the date of the meeting a statutory report containing the prescribed information must be sent to all members.

The object of the statutory meeting is to provide the shareholders with an early opportunity of inquiring into the conduct of the promotion, ascertaining the position of the company in relation to its membership and the working capital required to carry on the business, and obtaining information with regard to the future prospects of the company.

At the statutory meeting the statutory report is considered and adopted and the members present have a right to ask any questions relating to the formation of the company.

(b) *Ordinary General Meetings.* The directors of a company must call a general meeting of shareholders once at least in every calendar year in order to present to them the annual report and accounts, a copy of which is circulated to them at least fourteen days before the date of the meeting. By means of the directors' report and the annual balance sheet and profit and loss account the members of a company are fully informed about the progress of their concern and about the manner in which it has been conducted by those representing their interests. The report and accounts supplied to the members contain sufficient material in order to enable them to form a correct opinion about the company's affairs.

The provision gives to the members an annual opportunity of reviewing the work of their agents and, if not satisfied with the results, of making criticisms on the running of his business. When all is well and profits are ample, company meetings are usually happy functions which last only for a few minutes. But when all is not well, and shareholders suspect that there has been incompetence on the part of the management, a company meeting may be anything but a happy gathering. Shareholders who have been deluded into losing their money are usually angry and often voluble.

The usual procedure at an ordinary meeting is for the chairman to address the meeting on the company's operations for the period under review, to explain the accounts, and sometimes to give an indication as to how the company is faring during the current year, and possibly to indulge in some mild prophecy. He then moves that the report and accounts be received and adopted.

The chairman's motion having been seconded, it is usual for him to invite questions from shareholders. It is then that dissatisfied shareholders may not only ask questions but also ventilate their views as to the manner in which the

company is directed, and make suggestions for the directors' and managing agents' consideration. Shareholders who are thoroughly dissatisfied with the management will sometimes take the extreme course of rejecting the motion for the adoption of the accounts. Such a course, however can have little or no practical effect unless it is accompanied by the appointment of a committee to investigate the affairs of the company, and an adjournment of the meeting until the committee has reported the result of its investigation. Regulation 105 of Table A, which is compulsory for all companies, gives to shareholders the power to obtain inspection of the books of account and vouchers of the company by appointing a committee for the purpose.

4. *Appointment of Inspectors* When shareholders are dissatisfied with the conduct of the company's affairs as revealed by the director's report and audited accounts and by the proceedings at ordinary meetings, they cannot override the powers of the directors and cannot force the directors to give information which in the directors' opinion might damage the company. In such circumstances, as stated above, they may refuse to pass the accounts at the ordinary general meeting and appoint a committee of shareholders to inspect the books of account and vouchers of the company and to make a report to the members at an adjourned meeting. This method can be useful only where the directors themselves have nothing to hide and are in sympathy with the committee, because there is no power given to such committee to examine witnesses on oath. Therefore this course is usually adopted only when matters are not serious enough to upset absolutely the confidence of the shareholders in the management. If, however, the matters to be investigated are of a more serious nature, the shareholders may adopt either of the two following statutory methods of investigation.

(a) Section 138 provides a means of investigation by inspectors who are appointed by the Provincial Government to carry out an investigation on behalf of shareholders on the application of members holding a specified proportion of the issued share capital, such proportion being one-fifth in the case of banking companies and one-tenth in the case of other companies having a share capital. In the case of a company not having a share capital, such application may be made by not less than one-fifth in number of the persons who are on the company register of members.

This is the strongest weapon in the hands of shareholders, for by it the past and present directors, officers and agents of the company may be made to produce to the inspectors all books and documents in their custody or power, and may be examined on oath in relation to the business of the company. The inspectors thus appointed will make their report to the Provincial Government in such form as it may direct, and one copy of the report will be sent by the Provincial Government to the Registrar and one copy to the company, and a further will, at the request of the applications for the investigation, be delivered to them.

All expenses of investigation are to be borne by the applicants unless the Provincial Government directs the same to be paid by the company.

(b) The other statutory method of investigation is provided by section 142, under which the shareholders may make the appointment of inspectors without having recourse to the Provincial Government. The appointment of inspectors must, however, be made by a special resolution of the company. The inspectors so appointed will make their report direct to the company and not through the Provincial Government; and they possess the same powers as the official inspectors.

5. *Complaint to Registrar.* Under section 137 (6), if any shareholder complains to the Registrar, by placing the necessary material before him, that the business of a company is being carried on fraudulently, the Registrar is authorised to make an investigation, and after inquiry is entitled to make a report to the Provincial Government.

According to section 141-A, the Provincial Government in proper cases has to take upon itself the duty, at the cost of the State, of launching prosecution of persons who may be believed to be guilty of any offence in relation to the company. A person so convicted is debarred for five years from taking part in the management of a company.

If, however, the Registrar after making proper inquiry is of the opinion that the complaint is false, he will disclose the identity of the complainant to the company, and the company may take legal proceedings against him for the recovery of damages.

6. *Other Powers of Shareholders.* The compulsory regulation 71 of Table A vests in the directors the entire powers of the management of a company's affairs except those that are expressly reserved by the Indian Companies Act and those that may be expressly reserved by the articles as belonging only to members of the company. There are thus a number of things such as the alteration of capital, the alteration of articles, the sale of the company's undertaking, the remission of a debt due by a director, the schemes of financial reorganisation, etc., which can be done only by the shareholders in general meeting by passing an appropriate resolution.

Conclusion. Described above are the legal methods by which the shareholders of a company may exercise control over its affairs. It must not, however, be overlooked that, harring a complaint to the Registrar which may be made even by a single shareholder, everything depends upon the members' commanding a majority of votes at general meetings at which any particular action is proposed to be taken by them. In practice, the shareholders seldom if ever succeed in securing the majority of votes for the reasons stated below:

(a) The directors of companies under managing agents are not independent bodies responsible to shareholders, because partners, friends, relations, brokers and solicitors of managing agents predominate on such Boards, mainly

owing to the defective method of appointing directors laid down in the articles. To begin with, the first directors are appointed by promoters who take care to choose the safest men. Secondly the managing agents themselves have the power to appoint the directors up to one third of their total number. Thirdly, the articles reserve a number of seats on the directorates for special interests, and these seats are invariably filled up by men of the managing agents' choice. Thus there is a permanent nominated block ever ready to side with the managing agents.

(b) In any fight with the shareholders the directors and managing agents put up a united front. It is well known that they generally possess and where they do not possess they easily make up the necessary voting strength, so that no resolution may be passed against them will. This is made possible partly by the apathy on the part of shareholders and partly by the manoeuvres of the management. Many shareholders do not vote either in person or by proxy; some are dead while many others are untraceable. Some reside at long distances often out of India while many others are disqualified from voting by reason of the shares not having been registered in their names. Thus the voting strength of shareholders is substantially reduced. Again long before any general meeting, the companies' officers and clerks are let loose to canvass for proxies which the management succeed in obtaining on one pretext or another with the help of the large patronage commanded by them. The contest between the shareholders and the management thus becomes one-sided in which the shareholders must lose. Thus, though the directors and managing agents may lose the confidence of shareholders, they continue to govern the affairs of the company with impunity.

Where, however, the shareholders of a company take an intelligent interest in the affairs of a company and can combine for a fight with the management, they can certainly succeed.

Private Companies

When the joint stock system was first introduced, it was generally believed that the joint stock method would be applied only to large enterprises, which could not get enough capital without approaching to a wide mass of shareholders. It was never intended that small businesses should be brought under the joint stock organisation, or should have the division of their ownership into transferable and publicly marketed shares, but rather that they should remain business partnerships without limited liability. But once the privilege of joint stock enterprise had been granted, it was impossible to confine it within these limits, and therefore for some time the use of the company structure by relatively small concerns was regarded as a breach of the spirit, though not of the letter, of the company legislation.

Nevertheless the number of small companies continued to increase, and ultimately they were recognised by law as private companies. Private companies were for the first time introduced in the Indian company law by the Indian

Companies Act of 1913. Prior to that they were on the same footing as public companies and did not enjoy the special privileges that are now conferred upon them.

Definition. A 'private company' is defined by section 2 (1) (13) as a company which by its articles (a) restricts the right to transfer its shares; and (b) limits the number of its members (exclusive of persons who are in the employment of the company) to fifty; and (c) prohibits any invitation to the public to subscribe for its shares and debentures—

Provided that where two or more persons hold one or more shares jointly, they shall be considered a single member.

A private company must, however, send with the annual return, which is to be filed with the Registrar under section 32, a certificate signed by an officer of the company that the company has not, since the date of the last return or in the case of the first return, since the date of incorporation, issued any invitation to the public to subscribe for any shares or debentures of the company, and if the annual return discloses the fact that the number of members of the company exceeds fifty, also a certificate so signed that the excess consists wholly of persons who are not to be included in reckoning the number of fifty.

Formation. A private company may be formed by filing with the Registrar only the memorandum and articles of association, statutory declaration and notice of registered office, and by paying the same duty and fees as are required to be paid by a public company. The memorandum of association of a private company may be signed only by two persons instead of seven as in the case of a public company.

There are no restrictions on the allotment of shares or the commencement of business by a private company. A private company can, therefore, start business immediately after incorporation.

Section 147 provides that, if the number of members of a private company is reduced below two and it carries on business for more than six months while the number is so reduced, every member during the time it so carries on business after those six months and is cognisant of that fact shall be severally liable for the payment of the whole debts of the company contracted during that time.

Legal Privileges. The legal concessions that are enjoyed by private companies as against public companies may be summarised as follows :—

1. In order to form a private company only two signatories to the memorandum of association are sufficient (Sec. 5).

2. A private company is not required to hold the statutory meeting or prepare the statutory report (Sec. 77).

3. It is not necessary that any of the directors of a private company should be subject to retirement by rotation (Sec. 83.B).

4. There is no restriction on the appointment and advertisement of the first directors of a private company (Sec. 84).

5. The managing agents of a private company may appoint more than

one-third of the total number of its directors (Sec. 87.1).

6. A private company is not required to file with the Registrar a statement in lieu of prospectus (Sec. 98).

7. There are no restrictions on the allotment of shares by a private company (Sec. 101).

8. A private company can start business or exercise its borrowing powers without any restrictions (Sec. 103).

9. A private company is not required to circulate its annual accounts to the members (Sec. 131) or to file them with the Registrar after they have been laid before its members at the ordinary general meeting (Sec. 134).

10. Holders of preference shares and debentures in private companies are not entitled to receive and inspect the audited accounts, unless so permitted by the articles (Sec. 146).

Besides the above mentioned privileges, the following further legal exemptions are granted to private companies so long as they are not subsidiary companies of any public company :—

1. Out of the regulations of Table A which are made compulsorily applicable to public companies under section 17, regulations 79-82 do not apply to a private company (Sec. 17).

2. The legal restrictions imposed on a public company in connection with financial assistance to be given for the purchase of its own shares does not apply to a private company (Sec. 54.A).

3. Certain statutory provisions with regard to company meetings and voting applicable to public companies are not imposed on a private company (Sec. 79).

4. A private company may have less than three directors (Sec. 83.A).

5. The prohibition on public companies in regard to the granting of loans or the guaranteeing of loans granted to directors does not apply to a private company (Sec. 86.D).

6. Restrictions imposed upon the power of management of the directors of a public company does not apply to the directors of a private company (Sec. 86-II).

7. It is not necessary that the managing agents of a private company should be appointed only for twenty years. They may be appointed for a longer period (Sec. 87.A).

8. The remuneration of the managing agents of a private company may be fixed in any way (Sec. 87.C).

9. The restriction on the granting of loans to managing agents does not apply to a private company (Sec. 87.D).

10. The prohibition on voting by interested directors is not applicable to a private company (Sec. 91.B).

11. The provision requiring an agent of the company, who makes a contract in his own name but on account of the company as the undisclosed principal to

make a memorandum of the contract and file it in the company's office, does not apply to a private company (Sec. 91-D).

12. A private company may employ an unqualified person as also any person in the employ of its director or officer as an auditor (Sec. 144).

Advantages. The legal definition of a private company and the various legal exemptions accorded to it make it a very suitable form of business organisation in certain circumstances. Since 1913 thousands of private companies have been registered in India, and the popularity of the private company is still increasing because it possesses the following important advantages :—

1. As the general public is not interested in the affairs of a private company, it is usually possible for the management to give their personal attention to its affairs. As a matter of fact, all the shares of a private company are generally held by a few persons who are often members of the same family. Thus the business is kept in the hands of the proprietors themselves and the results are in conformity with the efforts put in.

2. A private company is a very convenient form of organisation, since it enjoys the blessings of a public limited company in the form of corporate finance and limited liability, and also those of a partnership in the shape of personal interest of the proprietors and freedom from publicity.

3. As a private company cannot invite the public to subscribe for its shares, its affairs are kept strictly private; but at the same time its members have the protection of limited liability.

4. A private company has the advantages incidental to incorporation, the chief being the continuance of the concern notwithstanding deaths or insolvencies of its members. Shareholders may come and go but no changes of individual membership affect the company's existence.

5. The borrowing facilities, especially by means of debentures, which is the incidence of all companies, are made available.

6. The simplification of arrangements as between the members and the concern, which, in the case of an ordinary partnership, would be extremely complicated, is made possible.

7. In recent years when the incidence of taxation on companies has been very high, the private company form of structure has been adopted by many concerns with a view to avoiding income and super taxes. This is made possible in the following manner :—

(a) Provided the company distributes to the members a reasonable proportion of its profits in a manner which will make these profits chargeable to super-tax in the hands of its members, any sums placed to reserves will escape super-tax; and (b) in a bad year, directors' fees may be paid so as to cause a loss to be disclosed by the company's accounts, thus enabling the company to escape taxation at the higher rate.

Private Company becoming Public. There are two ways, as provided in section 154, in which a private company becomes a public company, namely—

4. A company has a legal entity apart from its members, with a perpetual succession of members, and is not dissolved, as is a partnership, by the death of a member.

5. The position arising upon the death of one member does not affect the financial position of the company itself as his shares must be transferred to some other person. In a partnership it may be necessary to utilise the resources of the firm to repay the amount due to the representatives of the deceased.

6. A member's interest in a company may be divided into several parts and bequeathed to persons who may not have the capacity or desire to undertake the duties and liabilities of partners.

7. When a business is converted into a company in consideration of shares, some of which are issued as payment for goodwill, the vendor is enabled, if he so desires, to sell part of his shares, and thus realise his goodwill without giving up his control of the business. Such a course is not possible in a partnership.

8. As already stated a private company possesses some income-tax privileges as compared with a partnership.

Disadvantages :

1. The initial expense involved in the formation of a company is greater than in a partnership.

2. Certain publicity attaches to the affairs of a private company particularly when it becomes the subsidiary company of a public company ; but a partnership is not subject to publicity of any kind.

3. Credit from suppliers to a partnership may be more generous than to a company owing to the limited liability of the latter.

4. A company is governed by the provisions of the Indian Companies Act, and even in the case of a private company, technical irregularities and breaches of the Act may accidentally arise and may entail expense and inconvenience. But there is no such thing in a partnership.

Guarantee Companies .

Companies limited by guarantee are usually formed for the purpose of carrying on mutual insurance business or they are trade protection societies, chambers of commerce, clubs or other associations in which it is not intended to make a profit. There are two kinds of guarantee companies, viz, (a) companies limited by guarantee and not having a share capital, and (b) companies limited by guarantee and having a share capital divided into shares of a named denomination.

Associations not for Profit. Under section 25, companies formed to promote commerce, art, science, religion, charity, or any other useful object, which do not propose to pay dividends but to apply all their profits towards the promotion of their objects, may register a name without the word "Limited," provided they obtain a license from the Provincial Government.

A Provincial Government may grant a license on such conditions and subject to such regulations as it may think fit. Such a company enjoys all the

privileges of limited companies and is subject to all their obligations except those of using the word 'limited' as part of its name, publishing its name, and of sending lists of members to the Registrar. The license may at any time be revoked by the Provincial Government, and on revocation, the company will cease to enjoy the above exemptions and privileges.

Such companies are usually formed as companies limited by guarantee not having a share capital.

Memorandum and Articles. According to section 7, the memorandum of association of a company limited by guarantee must state (i) the name of the company with "Limited" as the last word in its name, (ii) the province in which the registered office of the company is to be situated, (iii) the objects of the company, (iv) that the liability of the members is limited, and (v) that each member undertakes to contribute to the assets of the company in the event of its being wound up while he is a member, or within one year afterwards, for payment of the debts and liabilities of the company contracted before he ceases to be a member, and of the costs, charges and expenses of winding up, and for adjustment of the rights of the contributories among themselves, such amount as may be required, not exceeding a specified amount.

If a company limited by guarantee has a share capital, the memorandum must also state the amount of share capital with which the company proposes to be registered and the division thereof into shares of a fixed amount, no subscriber of the memorandum shall take less than one share, and each subscriber shall write opposite to his name the number of shares he takes.

The guarantee clause in the memorandum of a company limited by guarantee is worded as follows:—"Every member of the company undertakes to contribute to the assets of the company in the event of its being wound up while he is a member, or within one year afterwards, for payment of the debts and liabilities of the company contracted before he ceases to be a member, and the costs, charges and expenses of winding up and for the adjustment of the rights of the contributories among themselves, such amount as may be required not exceeding one hundred rupees."

In the case of a company limited by guarantee, it is required by section 17 that articles must be registered with the memorandum. The articles must state the amount of share capital or the number of members with which the company proposes to be registered.

The memorandum and articles of a company not for profit registered under section 26 are exempt from stamp duty. The memorandum of such a company must, however, contain a statement to the effect that the income and property of the company shall be applied solely towards the promotion of its objects and no portion thereof shall be paid or transferred, directly or indirectly, by way of dividend, bonus, etc., to the members of the company; and a statement that the foregoing provision is a condition on which the license has been granted by the Government.

If a company limited by guarantee and having a share capital goes into liquidation, every member of it is liable to the extent unpaid on his shares, in addition to the amount he has undertaken to contribute in the event of a winding up.

Termination of a Company's Existence

A joint stock company, being a creature of law, cannot die a natural death; but it does not mean that its existence is necessarily perpetual. It is created by law and it is effaced by law. There are three distinct ways in which a company's personality is dissolved, viz—(a) By winding-up; (b) By its name being struck off by the Registrar; and (c) By being dissolved by an order of the Court.

(a) *Winding-up.* The commonest method of terminating the existence of a company is by means of winding-up. A company may be wound up for the purpose of reconstruction or for the purpose of definitely closing down its business. There is no such thing as insolvency for a company. A company may compound with its creditors and continue business, but it cannot, like an individual, have its affairs liquidated and then receive a discharge enabling it to resume business.

The law relating to the winding up of companies is contained in sections 155-245. There are several different kinds of winding up. A company may be wound up by the Court, or voluntarily, or subject to the supervision of the Court. A voluntary winding up, if the majority of the directors file with the Registrar a declaration of the company's solvency (such declaration being supported by a report of the company's auditors on the company's affairs), is called a members' voluntary winding up. If such a declaration is not filed, the winding up is called a creditors' voluntary winding up, and the legal provisions relating to the proceedings contain much more stringent protection for the creditors.

The most drastic winding up of all is winding up by the Court, usually known as compulsory winding up. Although the winding up by the court is called compulsory, the initiative for it may be taken by a resolution of the company itself to the effect that the company shall petition the court for a winding up order. More usually, however, the initiative is taken by a creditor on the ground that the company is unable to pay its debts. While insolvency is the usual ground for a petition for compulsory winding up, there are other grounds on which the court may make a compulsory winding up order. It may do so, for instance, if it is of the opinion that it is just and equitable that the company should be wound up—a phrase that covers a multitude of reasons.

The winding up of a company under the supervision of the court is comparatively rare, as the interests to be served are more adequately met by one of the other forms of liquidation.

(b) *Name Struck off by Registrar.* Where a company has in fact ceased to pursue the object for which it was constituted, there is no justification for preserving its formal entity by maintaining the registration of its name with the Registrar. It is accordingly provided in section 217 that where the Registrar

has reason to believe that a company is not in operation or carrying on business he will make inquiries from the company, and, if he finds that the company is really defunct, he will publish a notice in the official gazette that after three months from the date of the notice the company's name will be struck off the register and the company will be dissolved.

(c) *Dissolution by Court* Where under section 153, a company enters into an arrangement of reconstruction or amalgamation entailing the transfer of its assets and undertaking to another company, the Court in sanctioning the scheme may make an order under section 153.A for the dissolution of the company without winding up. This provision merely takes account of the fact that in the reconstruction of the company it is usually desired to preserve the undertaking and the assets including the goodwill of the company to be dissolved, so that liquidation of its affairs is not only unnecessary but contrary to the nature of reconstruction. The reconstruction of a company is thus made possible without winding up.

Test Questions

1. How are directors of joint stock companies selected and appointed in India? *(Agra B. Com. 1916).*
2. While selecting the directors of a Luga cotton mill company, what factors would you weigh in order to achieve the best results? *(Bombay B. Com. 1937).*
3. What are the duties and powers of a company director under law? Explain clearly. *(Agra M. Com. 1947).*
4. Discuss the law relating to the removal of and the vacation of office by a director. *(Agra B. Com. 1948).*
5. What are the influences which help to increase the concentration of power in the hands of the directors of a joint stock company? *(Bombay B. Com. 1935).*
6. What is the meaning of a managing agent? What are his functions in the running of a joint stock company? *(Cal. B. Com. 1916)*
7. Critically examine the part played by the managing agency system in the development of Indian industry. *(Bombay B. Com. 1946).*
8. Examine the influence of the managing agency system on the structure to industry in India. *(Bombay B. Com. 1942).*
9. Discuss the merits and defects of the managing agency system of organisation and control of a joint stock company. *(Agra B. Com. 1942).*
10. Discuss the part played by managing agents in financing the industries in this country. Do you consider it essential under modern conditions? *(Agra B. Com. 1918).*
11. What influences have operated in giving managing agents enormous powers of control over the industrial concerns managed by them? *(Bombay B. Com. 1935).*

12. What are the advantages and disadvantages of a system of management when a managing agency firm manages a number of different companies.

(Bombay B. Com. 1941)

13. How far has the Indian company law done away with the drawbacks of the managing agency system in this country ?

(Bombay B. Com. 1939).

14. Assess the present position of managing agents in India. What do you think their future ?

(Bombay B. Com. 1944).

15. The managing agency system has outlived its utility in India. Do you share this view ?

(Cal. M. Com. 1945)

16. In what ways may the shareholders of a limited company exercise control over its affairs, and to what extent is their control real in this country ?

(Agra B. Com. 1945).

17. In a joint stock company what control is exercised and what responsibilities are borne by (a) shareholders, (b) directors and (c) managing agents ?

(Bombay B. Com. 1934).

18. How far in India generally the control of directors over the management is effective and the responsibility of the directors to the shareholders is real with special reference to the system of managing agents ?

(Bombay B. Com. 1937).

19. How far are risk and control associated in the working of the joint stock concerns in India ?

(Bombay B. Com. 1941).

20. What are the rights of the shareholders of a joint stock company ? How far do these rights enable the shareholders to secure control over the affairs of the company ?

(Bombay B. Com. 1941).

21. What are the advantages which the proprietor of a private business may secure by converting it into a private limited company ?

(Agra B. Com. 1946).

22. Discuss the relative merits of a partnership and a private company as forms of business organisation.

(Agra B. Com. 1943).

23. Explain the particular features and privileges of a private limited company as compared with a public limited company.

(Bombay B. Com. 1947).

24. Describe briefly the mechanism by which resources employed in industry are provided by persons or agencies not in actual control of policy.

(Bombay B. Com. 1935).

25. Set out the main differences between a partnership firm, a private limited company and a public limited company.

(Cal. B. Com. 1946).

CHAPTER 5

COMPANY SECRETARIAL WORK

Company secretarial work consists of the organisation of the secretarial department; maintenance of the statutory and other books, preparation and filing of the various returns required by the Indian Companies Act; writing up minutes of board and general meetings of the company, issuing notices, reports and circulars to shareholders, conducting correspondence with shareholders in regard to share allotment, calls, forfeiture, etc., transfers of shares, payment of dividends, and reorganisation and reconstruction schemes. If a company does not maintain a separate accounts department, the keeping of books of account, preparation of accounts for publication and arrangement for their audit, and also the taxation work of the company are also included in the secretarial department.

The person who is responsible for the secretarial work may be called the secretary of the company; but it is not necessary that he should be always called secretary. In India, a very large number of companies are managed by managing agents. Such companies have no such official as secretary, because all the secretarial work is done by the managing agents. Similarly in many banking and insurance companies, the secretarial work is in charge of a director, managing director, manager or general manager. The name is immaterial; function is everything. Whoever is responsible for the secretarial work of a company is the secretary, by whatever name called. Some managing agents call themselves as agents and secretaries or simply secretaries.

The position of a company secretary is not defined by law, though both specifically and by implication he is frequently indicated in the Indian Companies Act and the Indian Income-tax Act as being liable to penalties if he fails to fulfil the statutory obligations imposed upon him. A secretary is a mere servant of the company. His position is to do what he is told, and no person can assume that he has any authority to represent anything at all. The secretary is, then, merely an employee and has no original authority. He derives his authority either expressly or by implication from the directors, but he plays an important part in the management of the company. The duties of the secretary will necessarily vary according to the nature and size of the company he serves. The secretary of an ordinary company may in addition to purely secretarial work, be expected to keep accounts and do all the correspondence and other clerical work. On the other hand, the secretary of a large company may be in charge of only the secretarial department with a number of assistants, thus occupying a position of importance second only to that of the directors. The work preliminary to the registration of a company is usually done by the

promoters, and it is only after a company has been incorporated that the secretary appears on the scene.

A company secretary should have a sound general education and a command of the English language, as all the company secretarial work is done in English. He should be thoroughly familiar with company, income-tax, business profits tax and other mercantile laws as well as any other laws affecting the business of his company. He should be a man of good judgment, tact, and experience. He should preferably have a technical knowledge of the particular business carried on by the company, as he may be consulted by his directors—and particularly by the chairman—on questions of policy and administration. In many cases the secretary is also approached from time to time for advice, opinion, or assistance in regard to the private affairs of the individual directors concerning investments, the preparation of reports and accounts for societies, clubs, social and religious organisations in which they are interested, and many other matters. Furthermore, the right kind of man will have unrivalled opportunities of contributing towards the efficiency and welfare of the staff as well as the advancement of his company's interests, and he will gain the confidence and respect of all with whom he may come in contact. The first portion of the word 'secretary' implies that he is the keeper of the secrets. He is a confidential servant of the company and he will be the recipient of much confidential information and, therefore, accidental or careless disclosure may have far-reaching consequences.

As a company secretary is personally liable for numerous penalties if there is default in the matter of complying with the requirements of the Indian Companies Act, it will be evident that his position is no mere sinecure. He must, therefore, be careful and methodical, and fully alive to his duties and responsibilities.

The secretary of a new company should, first of all, organise his department systematically. The head of any office should 'have been through the mill,' because such a position cannot properly be filled by one who has not himself experienced and overcome all the doubts and difficulties of the 'rank and file.' The ideal to be kept in view in any well-organised department of a business concern is the maximum of efficiency combined with the minimum of waste, but the chief point to be observed in order to attain an all-round happy and cheerful cooperation is a minimum of friction among individual workers. Workers are but human. The man who has got a specialised job or who is assigned a position of definite responsibility, and who carries out his duties ably and conscientiously has his own point of view on the dignity of his office, and this being so, any unnecessary interference by others is tactless. The secretary has full scope for the exercise of his training and character as he is able to bring to bear upon the administration of his office that broadness of outlook and tactful diplomacy which are so essential to the *esprit de corps* of its personnel:

The power to read character is an mean factor in commercial success, and

a secretary who is imbued with such a gift will find it invaluable when organising his staff. He will be interested in them and will lend a sympathetic ear to their views and opinions. If he sees that they work well he is also mindful of the fact that they should play hard—a sound mind in a sound body. There is no fun like work, but play is an inviolable tonic. It may be stated that 'system' is simply organised common sense. It implies capability for the work in hand so that it is done thoroughly and with a minimum of energy. It ensures speedy and accurate reference to any detail of the work at any time. It does not, however, entail elaborate records and an excessive staff. That is system run riot.

Having arranged his Office, he should attend to the following matters :—

(a) The name of the company must be kept painted or affixed in letters easily legible, and in a conspicuous position on the outside of every office or place where the company carries on business

(b) The name of the company must be engraved in legible characters on its common seal.

(c) The name of the company must be mentioned in legible characters in all notices, advertisements, and other official publications of the company, and on all bills of exchange, hundis, promissory notes, endorsements, cheques, etc., purporting to be signed on behalf of the company and on bills, invoices, receipts and letters of credit of the company.

(d) He should arrange for a notice board to be set up in a conspicuous part of the office, and should see that all notices and other published information of interest to the members and to the public are displayed thereon for such period as may be considered sufficient.

The various duties, which a company secretary has to perform, will now be considered in detail.

Issue of Capital

Upon incorporation, the first necessity is to obtain the capital of the company, and this may be arranged privately or by public subscription. A company having an authorised capital of more than Rs 5,00,000 cannot, however, issue its shares unless it has first obtained the written consent of the Central Government under the Capital Issues (Continuance of Control) Act, 1947. Where capital is to be raised by public subscription, a prospectus is issued for the purpose, and with the prospectus application forms are enclosed. Applicants for shares must send these forms duly filled in with the application money, to the company's bankers. This is the usual practice where the issue is one of any magnitude, but in some cases it may be deemed convenient for the company to receive the forms and the application money at its own office or at the office of its managing agents.

Listing of Application Forms. All the application forms received by the company either direct or through its bankers should be carefully checked in order to see that the amount paid on application is correct and that each form is

properly filled up and signed. They are then listed on separate sheets called "Application and Allotment Sheets". Where the issue is large and there are many applications, it is better to arrange the application forms alphabetically and use separate sheets for each letter of the alphabet. In this way, the work may be divided amongst several clerks. Each sheet is separately totalled and final summary sheet compiled to record the totals of the separate sheets. After the allotment is completed, the sheets may be bound in book form for permanent record.

The following is the ruling of an Application and Allotment Book.

Application and Allotment Book

Left-hand Ruling—

Application No.	Allotment No.	Name	Address	Occupation	Shares applied for	Paid on Application Rs.	C. B. Folio	Remarks

Right-hand Ruling—

Shares allotted	Distinctive Nos. from to	Total due on application and allotment Rs.	Balance due on allotment Rs.	Date of payment	Amount refunded Rs.	C. B. Folio	Register of Members Folio	Share Certificate No.	Remarks

The Allotment. When the minimum subscription has been obtained and the list is closed, a meeting of the directors will be held to consider the applications and to make the allotment. The Application and Allotment Sheets should be initialled by the chairman of the company. A minute of the directors' resolution of allotment must be recorded in the Directors' Minute Book. This resolution may be as follows :—

"RESOLVED that the number of shares entered in the column headed 'Shares Allotted' of the Application and Allotment Sheets against the name and address of each applicant, be allotted to each applicant, making a total allotment of shares, and that a letter of allotment, stating particulars of the shares allotted and the amount payable on allotment, be sent to each allottee; and where no number of shares is entered in the 'Shares Allotted' column against the applicant's name, that no allotment be made, and that the application money be returned to each applicant with a Letter of Regret."

If the allotment is not made within 180 days after the first issue of the

prospectus the whole of the application money received must be returned within the next ten days to the applicants.

A company prospectus is an invitation to the public to make offers for its shares, the applications sent in by prospective shareholders are offers made to the company, and the allotment made by the company is the acceptance of those offers. Therefore any applicant may withdraw his application and be entitled to a return of the money deposited at any time prior to the posting of the letter of allotment. The posting of the letter of allotment, however, completes the contract which then becomes irrevocable, and any subsequent notice of withdrawal has no effect. A record of the posting of allotment letters should be kept in the company's office.

Letter of Allotment. On the allotment of share being formally made by the directors, particulars of allotment should be recorded in the Application and Allotment Sheets, and a letter of allotment should be sent to each allottee. The allotment letters, which should bear a two-anna revenue stamp, should be carefully prepared from the Application and Allotment Sheets and fully checked before they are dispatched to the allottees at their addresses as given in the application forms. The following is a specimen letter of allotment:—

The Swadeshi Company Ltd.

25, Civil Lines,

Agra, 15th March 1919

Name and Address of
Allottee.

Dear Sir, Madam,

In response to your application dated you have been
allotted.....Shares of Rs each in the Swadeshi Company Ltd.

The amount payable on Application and Allotment at Rs.... ..per share,
Rs.

You have already paid

Amount due from you on Allotment ... Rs.

Payment of the amount due from you should be made on or before

..... to

Yours faithfully,

.....
Managing Agents.

This form, with remittance, must be forwarded entire to
who will return it duly receipted. It should then be carefully preserved to be
exchanged for the relative Certificate in due course

Oversubscription. If the shares offered for public subscription are oversubscribed some applicants may be allotted the full number of shares applied for, some may be given a smaller allotment, while some may not be allotted any shares at all. In such cases it is customary to appropriate the excess application money towards the amount due on allotment and to refund the balance, if any.

Letter of Regret. If the issue is oversubscribed, and to some of the applicants no allotment is made, a letter of regret somewhat in the following form should accompany the cheque returning the application money.

The Swedeshi Company Ltd.

25, Civil Lines,

Agra, 15th March 1949.

Dear Sir/Madam,

We have to inform you that the Directors regret that they are unable to allot you any shares in this Company in response to your application dated

We therefore enclose a cheque for Rs., being refund of the amount paid by you on application. Please acknowledge receipt.

Yours faithfully,

Enclos : Cheque.

Managing Agents.

Return of Allotment. Within one month from the date of allotment there must be filed with the Registrar a return of allotment in the prescribed form, stating.

- (a) The number and nominal amount of the shares allotted, distinguishing the various classes of shares ;
- (b) The amount due or payable on each share ;
- (c) Particulars of the shares allotted for a consideration other than cash, and the amount treated as paid on each share ; and
- (d) The names, addresses, and descriptions of the allottees.

The contract constituting the title of the allottee to shares allotted for a consideration other than cash must also be filed with the Registrar ; and if the contract is not reduced in writing, particulars of the contract, duly stamped according to its nature, must be filed.

Register of Members. When the allotment of shares is completed, the necessary entries must be made in the Register of Members, in which a separate account of each member is to be kept.

Calls

How call is made. It is not usual for shares to be issued subject to the whole of their nominal value to be paid in one lump sum. In most cases of public issue, a certain amount (which under section 101 must not be less than 5 per cent) is payable on application, a further sum on allotment, and either the balance is made payable at some subsequent fixed date (sometimes by several instalments falling due at different dates), or the shares are left partly paid. The directors are empowered by the articles to demand a settlement of the outstanding liability on shares as and when they deem fit. Such a demand made by directors is known as a "call". It must be made by means of a resolution of the board of directors, and should be notified to the shareholders concerned.

Provisions restricting the amount for which any single call may be made and prescribing an interval of time which must elapse between one call and another, are inserted in the articles of many companies. The secretary should, therefore, be careful to consult the articles of the company whenever a call is made in order to make sure that no regulation bearing on the matter is overlooked.

As a rule, a call is deemed to have been made at the time when the resolution of the directors is passed, and the persons who then held the shares in respect of which the call is made, are liable to pay the same.

Call List. A list of members should be prepared on the lines of the specimen shown below. Each member should be allotted a consecutive number which should appear on the call letter.

Call List

First call of Rs. 20 - per share on Ordinary Shares due on.....

No.	Name	Address	No. of Shares	Polo	Amount due Rs.	Date paid	Amount paid Rs.	Remarks.

This list is written up from the Register of Members. The amount due from the members as shown by the Call List should be totalled, and checked with the total amount due in respect of the call, to ensure that there are no errors.

Call Letters. When the call list has been prepared and duly checked, call letters for shareholders must be written up. The call letters should then be issued in accordance with the regulations of the articles for the giving of notices to members, and a record of the posting of these letters should be preserved for future reference. The manner of giving notices to shareholders is explained later on. The following is the form of a specimen call letter.

The Swadeshi Company Ltd.

No... ..

25, Civil Lines,
Agra.

.....

.....

.....

.....1919.

Dear Sir/Madam,

We have to inform you that the directors by a resolution of the Board dated.....have made a call of Rs... ..per share on the.....Shares of the Company, making these shares fully paid/paid up to the extent of Rs.per share.

The amount due from you in respect of the.....shares registered in your name is Rs.....which amount must be sent on or before....., together with this entire notice, to the Company's bankers,Bank, Ltd., Agra, or to any branch of the Bank, which will return the notice duly receipted.

This Call Letter, when duly accepted, should be carefully preserved, as it will have to be surrendered subsequently when the share certificates are issued, and a further communication in this connection will be sent to you in due course.

Yours faithfully,

.....
Managing Agents

Receipt of Money in Payment of Calls. Calls may be made payable at the company's office, but, as a rule, it is found more convenient to arrange for payment to be made to the company's bank by whom a cash receipt is issued. The form for this receipt is attached to the call letters, which should be surrendered entire when the payments are made.

Register of Members. Immediately a call is made, the cash account of each member in the Register of Members should be debited with the amount due, and the various accounts should be duly credited when payments are received from the members in respect of the call.

Share Certificates. Share certificates usually state the amount which has been paid up on the shares, and where such are partly paid, provision is made on the certificates for the endorsement of subsequent payments. In such cases, members should be requested at the time the call is made to lodge their certificates, accompanied by the banker's receipt, at the company's office for endorsement.

✓ Forfeiture of Shares

It may be noted at the outset that the Indian Companies Act of 1913 is, with the exception of section 32, silent on the question of forfeiture of shares. This section requires particulars of the total number of shares forfeited to be included in the annual return. Therefore shares cannot be forfeited unless the articles of the company expressly provide for forfeiture. If the company has not expressly excluded regulations 24-30 of Table A, the company has that power. If, on the other hand, the articles do not authorise forfeiture, the company must either alter its articles to give it the necessary power or else obtain the sanction of the court for the purpose.

Shares can be forfeited only in respect of unpaid calls or instalments as provided by the articles. Shares cannot be forfeited for a trading debt, as such action would be tantamount to a purchase by the company of its own shares. Further there must be no forfeiture other than for the benefit of the company.

The articles laying down the procedure in regard to forfeiture must be strictly followed if the forfeiture is to be valid, as the only authority permitting forfeiture is the contract with the member contained in the articles.

The procedure on forfeiture depends on the articles, and the following is an outline of the procedure based on Table A :—

1. The directors pass a resolution that a notice be given to the shareholder in default, requiring payment of the call with interest on or before a

certain date (being not less than 11 days from the date of the notice) and informing him that otherwise the shares will be forfeited. This notice should be sent by registered post.

2. If the shareholder fails to comply with the notice, the shares may be forfeited, and if that course is decided on, the directors pass a resolution forfeiting the shares. The resolution must be validly passed at a properly constituted meeting, and a copy thereof may be sent to the member. This resolution may be as follows :—

"RESOLVED that 100 shares of Rs. 10 each numbered 650-749 inclusive, whereon Rs. 7 a share has been paid and which at the date of this resolution were standing in the name of Mr. of, who has failed to comply with the notice served upon him dated the, be, and they are hereby forfeited for non-payment of the final call of Rs. 3 a share made on the.... and for non-payment of interest thereon, and that the said shares be disposed of as the directors think fit in the best interests of the Company."

3. An entry should be made in the defaulting member's account in the Register of Members to the effect that the shares have been forfeited by a resolution of the directors. The date and number of the resolution would be included in the entry. His account would then be closed by transferring the shares forfeited to a 'Forfeited Shares Account' in the Register of Members where they would remain pending the reissue.

Reissue of Forfeited Shares. On forfeiture, shares become the property of the company, and can be sold for whatever they will fetch, provided that the company receives altogether from the ex-shareholder and the purchaser the same amount as is paid up in respect of other shares of the same class. In other words, forfeited shares may be sold at a discount not exceeding the amount paid up at the time of the sale.

The procedure on reissue of forfeited shares depends on the articles. According to Table A, it is as follows :—

1. A director makes a duly verified declaration in writing setting forth details of the shares, and the date on which they were forfeited, and declaring that the shares were duly forfeited on that date.

The effect of this statutory declaration is that it is conclusive evidence against all persons claiming to be entitled to the shares, as it can be appreciated that, in the event of the company not being able to regain possession of the share certificate from the defaulting member respecting the forfeited shares, there would be two share certificates in existence for the same block of shares when the forfeited shares were reissued or sold and a new certificate issued.

2. In order to vest the shares in the purchaser, the directors pass a resolution in the following form :—

"RESOLVED that the 100 shares of Rs. 10 each, Rs. 7 per share paid up, numbered 650-749 inclusive, having been duly forfeited by a resolution of the

Board dated....., be reissued to Mr.....of.....as fully paid, at Rs. 6 per share, representing the unpaid final call of Rs. 3 per share and Rs. 3 per share premium; that the Seal of the Company be affixed to the transfer of the said shares to the said Mr.....; that the said transfer be and is hereby passed for registration; and that a certificate for the shares is the same of Mr.....he duly sealed and signed."

3. The shares are then transferred from the "Forfeited Shares Account" to the name of the purchaser in the Register of Members, and a Share certificate issued to him.

An ex-member whose shares have been forfeited, is not liable as a shareholder, and he escapes the payment of all further calls, unless the articles of the company provide otherwise. If the articles do so provide he may be liable as a debtor for the amount of his unpaid calls so long as they remain unpaid, unless the company's right of action becomes time-barred. But if a company is wound up within a year after forfeiture, such former member may be placed upon the "B" list of contributories if the assets are insufficient to meet the claims of creditors.

Articles frequently provide that members whose calls are in arrear shall be precluded from attending and voting at meetings of the company.

Cancellation of Forfeiture. If the articles so permit, the forfeiture of shares may be cancelled on such terms as the directors think fit. The directors will pass a suitable resolution for the purpose, the ex-member informed accordingly, and his account will be restored in the register of Members.

Share Certificates

Section 29 provides that a certificate, under the common seal of the company, specifying the shares held by a member, shall be *prima facie* evidence of the title of the member to the shares therein specified.

A share certificate is a document of title which is issued by a company to every shareholder. It states the name of the person to whom it is issued, the number of shares it represents, the distinctive numbers of and the amount paid on such shares. It must be sealed with the common seal of the company and bear a stamp of two annas. The share certificate is usually in the following form:

The.....Co., Ltd,

This is to certify that Mr.....of.....is the registered holder of.....shares of Rs.....each, numbered.....to..... inclusive, in the above-named Company, and the sum of Rs.....has been paid up on each of the said shares.

Given under the common seal of the said company this.....day of.....
.....Director

Seal

.....Secretary

Section 29 provides that a certificate under the common seal of the company

shall be *prima facie* evidence of the title of the members to the shares. A share certificate is thus only *prima facie* evidence of the title of the member to the shares, but it is not of itself conclusive evidence of title. Therefore, it may be rebutted by a company, for example, in the case of a person who has obtained the share certificate by means of a forged transfer. But where a person acquires the shares in good faith and for value, the company is estopped from denying the truth of any statement contained in the certificate.

Section 108 requires that share certificates must be ready for delivery within three months after allotment or after registration of a transfer, unless the terms of the issue of shares provide otherwise. Therefore, if it is the intention of the company not to issue share certificates until the shares are fully paid, and if all the calls due on the shares are not payable within three months after allotment, the prospectus must contain a clause that the share certificates will only be ready, say three months after the date on which the final call is payable.

Preparation of Share Certificates. Share certificates are written up from the Register of Members, and great care should be taken in their preparation. Where a share certificate is issued for only partly paid up shares, it must clearly state the amount paid up on each share. Such a certificate usually provides on its back suitable and sufficient space for endorsing further payments of calls. If it is the intention of the company to create a reserve liability, the fact should be clearly mentioned on the face of each share certificate. When the share certificates are ready, they will be sealed under the authority of a resolution of directors.

Delivery and Despatch of Share Certificates. Share certificates are usually, delivered against surrender of some temporary document such as a letter of allotment or a transfer receipt, etc. If the exchange is effected personally at the company's office, either by the shareholder or by his agent, the signature of the person receiving the certificate should be obtained on the document surrendered. Certificates should be forwarded by post only on the understanding that they are sent at the risk of the shareholder.

Lost Share Certificates. The articles commonly empower the directors to issue new certificates to replace any that may have been lost or stolen, it being left to the discretion of the Board to decide what formalities must be complied with before the issue of a duplicate is sanctioned. Before a duplicate share certificate is issued to a shareholder, the usual procedure is as follows:—

1. The shareholder has to deliver to the company a statutory declaration, setting forth the true facts and narrating the circumstances, accompanied by the prescribed fee for the issue of the duplicate certificate and a letter of indemnity indemnifying the company against any claims, losses or expenses that may be incurred either through the original certificate having been lost or mislaid or by reason of the issue of a new certificate. The following is the specimen text of a letter of indemnity to be addressed by the shareholder to the company:—

"In consideration of your having issued to me a duplicate share certificate for ten fully paid ordinary shares of Rs. 100 each numbered 375 to 384 inclusive in place of the original share certificate for the said shares previously issued to me and which has been lost, I hereby undertake to indemnify you against all costs and expenses which you may incur in consequence of the aforesaid duplicate certificate."

2. The shareholder may also be required to bear the cost of giving a public notice of the loss in the newspapers. This notice may be as follows :—

The Swadeshi Company Ltd.

NOTICE is hereby given that an application has been made to the directors of this Company for the issue of a duplicate share certificate in respect of ten ordinary shares numbered 234-243, standing in the name of on the statement that the original certificate No. 87 has been lost.

If no objection is received within one month from this date, the directors will proceed to deal with this application.

By Order of the Board,

Agra, 3rd March 1949.

.....
Managing Agents.

3. If no objection is received in the company's office, the directors will sanction the issue of a duplicate share certificate. The new certificate should be marked "Duplicate" and an entry of its issue made in the Register of Members. In the event of the shareholder disposing of his shares, it is essential to see that the duplicate certificate is lodged with the transfer. If the original certificate is lodged with the transfer and not the duplicate, inquiries must be made as to the reason therefor, and the duplicate certificate must be surrendered before the transfer is passed for registration.

Circumstances when Share Certificates are issued. A Company issues share certificates in the following circumstances :—

1. *In exchange for letters of allotment and cash receipts, if any, when shares are offered to the public.*
2. *On the registration of a transfer of shares.*
3. *In respect of shares acquired by a person in consequence of the death or insolvency of a member.*
4. *In exchange for a worn out or defaced share certificate.*
5. *In respect of a share certificate which has been lost, mislaid, destroyed or stolen.*
6. *When a share certificate is to be split up, i. e. when a certificate for a certain number of shares is surrendered and two or more certificates are required, each for a part of the holding.*

Share Warrants

A public company limited by shares may, if so authorised by its articles and in respect of fully paid up shares, issue under its common seal a warrant called a 'share warrant', entitling its bearer to the shares or stock therein

specified, and providing by coupons or otherwise for the payment of future dividends. The share warrant entitles its bearer to the shares or stock therein specified and the shares or stock may be transferred by delivery of the warrant. The bearer of a share warrant, if the articles so provide, may be deemed to be a member of the company, but he shall not be qualified to be a director in respect of the shares included in the warrant. According to compulsory regulation 116 of Table A, notices of general meetings have to be given to holders of share warrants by means of advertisement.

On the issue of a share warrant, the company shall strike out of its Register of Members the name of the member then entered therein, and shall enter in the register the following particulars, namely:—

- (a) The fact of the issue of the warrant,
- (b) A statement of shares or stock included in the warrant, distinguishing each share by its number, and
- (c) The date of the issue of the warrant.

Till the warrant is surrendered these particulars shall be deemed to be particulars required by the Act to be entered in the Register of Members.

The bearer of a share warrant may, subject to the articles, surrender it for cancellation and have his name entered as a member in Register of Members.

If any registered holder of shares desires to exchange his shares for share warrant, he is usually required to make a written application to the company accompanied by his share certificate and the necessary stamp duty and the prescribed fee. On the application being approved by the directors, a share warrant will be issued to him and his name will be removed from the Register of Members.

Debentures

Borrowing by means of an issue of debentures is a method commonly adopted by companies for raising more capital. A debenture may be defined as a document issued by a joint stock company as evidence of its liability to repay money raised in addition to the share capital, and if it purports to give a charge it creates the security for repayment of the loan.

Issue of Debentures. The issue of debentures should not be completed until such time as the company is entitled to commence business in accordance with the provisions of section 103. The section permits, however, the simultaneous offer for subscription or allotment of shares and debentures, and the receipt of money payable on application for debentures.

Before deciding on an issue of debentures the directors must see that they are acting within the powers of the company as defined in its memorandum of association, although power to borrow is sometimes to be implied from the nature of the business carried on. The articles must also be consulted to see if there are any restrictions as to the amount which may be borrowed or the formalities to be carried out before the borrowing powers can be exercised.

An issue of debentures is effected much in the same manner as an issue of

shares. A prospectus is usually published inviting subscriptions. Application forms, allotment letters, etc., are used, and the procedure relating to the issue of capital applies more or less to the issue of debentures.

Registration of Charges. Section 109 requires that particulars of any mortgage or charge created for the purpose of securing an issue of debentures, together with the instrument by which the mortgage or charge is created or evidenced, should be filed with the Registrar within twenty-one days of the creation of such charge. If this is not done, the mortgage or charge is void so far as any security on the company's property is thereby conferred.

Particulars of all mortgages or charges specifically affecting the company's property should also be entered in the company's own register of mortgages and charges.

Conditions Governing Debentures. The conditions governing the issue of debentures are usually printed on the back of each debenture. The secretary must carefully peruse these conditions and see that the company faithfully carries out its obligations. The conditions may, inter alia, provide for the transfer of debentures, method of paying interest, regulations governing meetings of debenture holders, and the circumstances in which the principal money may become payable.

Register of Debenture holders. Debentures are usually issued in the form of registered debentures, or debentures payable to bearer with interest coupons attached, or debentures payable to bearer with interest coupons and with the right of conversion to registered debentures. Where a company issues registered debentures, particulars of the same will have to be entered in the Register of Debenture holders, a book, though not required by law, is nonetheless necessary.

Transfer of Debentures. A bearer debenture is transferable by mere delivery and there is nothing to be done about it in the company's office. But the transfer of registered debentures is to be effected by means of a transfer deed in the same way as a transfer of shares.

Redemption of Debentures. Debentures may be redeemed on a specified date or by periodical drawings. Whenever any debentures are redeemed, section 121 requires that an intimation should be given to the Registrar within twenty-one days from the date of payment.

Transfer of Shares

The right to transfer is conferred by section 28 which provides that the shares or other interest of any member in a company shall be moveable property-transferable in manner provided by the articles of the company. Unless the articles provide for the restriction of this right, directors are compelled to register all transfers submitted to them. The articles, however, commonly restrict the right to transfer. For example, directors are usually authorised to decline a transfer without giving any reason, or to refuse registration of a transfer of shares upon which the company has a lien, or to decline registration of a transfer

of partly-paid shares to a person of whom they do not approve. With private companies, the restriction of the right to transfer shares is a statutory necessity.

The transfer of shares is governed by the provision of the articles subject to the requirements of section 31. The usual procedure relating to transfer may be outlined as follows :—

✓ **Transfer Deed.** It is not lawful for a company to register a transfer of shares unless the proper instrument of transfer duly stamped and executed by the transferor and the transferee has been delivered to the company along with the scrip. But where it is proved that an instrument of transfer has been lost, the directors may, on an application in writing made by the transferee and bearing the necessary stamp, register the transfer on such terms as to indemnity as they think fit. Below is given a specimen instrument of transfer.

I, of, in consideration of the sum of Rupees.....paid to me by.....of
 (hereinafter called "the said transferee") do hereby transfer to the said transferee the share (or shares) numbered.....in the undertaking called.....Company, Limited, to hold unto the said transferee, his executors, administrators and assigns, subject to the several conditions on which I held the same at the time of the execution thereof, and I, the said transferee, do hereby agree to take the said share (or shares) subject to the conditions aforesaid

As witness our hands the..... day of.....

Witness..... Transferor.....

Witness..... Transferee.....

The instrument of transfer is to be properly executed (i. e., signed by both the transferor and the transferee in the presence of witnesses, who must attest the signatures of transferor and transferee). The witnesses must be independent persons and not relatives of transferor and transferee. The instrument should also bear the requisite stamp. Stamp duties differ in different provinces in India.

Where the transferor transfers the whole of his holding, he would hand over the share certificate to the transferee along with the transfer deed, but when he disposes of only a part of the shares represented by the share certificate, he would not deliver the certificate to the transferee, nor would the transferee be satisfied unless he were given the relative share certificate. This difficulty is got over in one of the two ways :—

✓ (i) Splitting of Shares Certificate. The transferor will send his certificate to the company's office for being split up into a number of certificates each for a specified number of shares. Most companies give this facility to their members on payment of a small fee. On receipt of the new certificates from the company, the transferor will hand over to the transferee an appropriate share certificate representing the exact number of shares sold.

(ii) Certification of transfer. The transferor may get the transfer deed certified. A certified transfer is one which bears a statement that the relative share certificate has been deposited with the company. The transfer form, executed by the transferor and with the transferee's name stated therein, is sent to the company's office accompanied by the share certificate for the whole holding. The share certificate is retained by the company and cancelled, while the transfer is certified by the secretary in the following manner :—

Certificate for.....shares Rs.....paid
lodged at the Company's office.

For.....Co., Ltd.

No

.....

Date

Secretary.

It is then returned to the transferor with a balance ticket for the remainder of the shares represented by the certificate. The transferor then delivers the certified transfer to the transferee, who after completing it lodges it with the company for registration. A balance ticket is a temporary certificate. It is accepted on the Stock Exchange and enables the transferor to deal with the balance of his holding. In due course, it is exchanged, on payment of a fee, for a share certificate.

In order to facilitate business, the Stock Exchange clearing house sometimes certifies transfers and forwards the certificates, accompanied by a list giving details of the transfers so certified, to the company's office. The transfers, when presented for registration, should be checked with this list and any material difference, e.g., alteration in name of transferee, advised to the clearing house authorities.

Scrutiny of Transfer Form. When completed, the transfer is lodged with the company either by the transferor or by the transferee, but usually by the latter. It must be accompanied (unless it is a certified transfer) by the share certificate, and the prescribed registration fee must be paid to the company. Before acceptance, the transfer must be carefully examined by the secretary to ascertain that it is complete and in correct form. It must be correctly stamped, dated, the company's name correctly given, the distinctive numbers of the shares correctly stated and in agreement with the numbers appearing on the share certificate, executed by both transferor and transferee, with their signatures properly witnessed, the description of the transferee stated, and finally the signature of the transferor compared with his signature when previously acquiring the shares. Alterations in the transfer should be initialled by both parties.

Transfer Receipt. When the transfer has been examined and found to be in order, a receipt would be sent to the person who lodged it. Such a receipt would state the date of its issue, the name of the person lodging the transfer, the number of shares, the distinctive number of shares, name of transferee, the fee paid, the date when the new certificate will be ready for delivery, and an indication as to whether the transfer was accompanied by a share certificate or had been certified.

cal meetings, or, as is more usual, by a standing Transfer Committee of the Board, whose proceedings are placed at the next Board meeting for confirmation.

When a transfer has been approved, the necessary entries are made in the Register of Members. The old share certificate is cancelled, and a new share certificate is made out in the name of the transferee and sent to him. In pursuance of section 108 the share certificate must be issued within three months from the date of registration of transfer.

No transfers are registered during the time the Register of Members is closed.

If the transfer is refused, a notice of the refusal must be given under section 34 both to the transferor and the transferee within two months from the date of lodgment of the transfer.

Effect of Transfer. The instrument of transfer is the authority for the company to alter its Register of Members, and its effect is that the member transfers all his rights and obligations as a member from the date of transfer. He does not transfer his rights to dividends or bonuses already declared, nor does he transfer liabilities in respect of calls already made; but he transfers his right to future payments and his liability to future calls.

The precise rights of the transferor and transferee (as between themselves) are, however, determined by the sale contract, and the sale may be with or without any dividend or rights attaching to the shares at the time of sale. Moreover, it may be arranged that the purchaser will pay an outstanding call.

The company is not a party to the sale contract and is, of course, unaware of its terms. Hence, the universal practice is to pay the dividends, at their due date, to the shareholder whose name is registered in the company's books. Where the transferee is entitled to the dividend, he must claim it from the transferor. If a call is outstanding, the common practice is to require the call to be paid before a transfer can be accepted for registration.

Blank Transfer. A blank transfer is a transfer in which the transferor hands over to the transferee the share certificate with transfer form completely blank but for the signature of the transferor. A blank transfer may be described thus. Upon a sale or mortgage of shares, the transferor very commonly signs and hands over what is called a blank transfer (i. e., transfer signed by the transferor but with a blank for the name of the transferee), the intention being that the purchaser or mortgagee shall be at liberty later on to fill up the blank and perfect his security by getting himself registered. The advantage of this is that the buyer is saved the trouble of signing two forms if he wants to sell the shares again. In the usual case, both the transferor and the transferee sign the transfer form and when the buyer wants to sell the shares he has to sign another transfer form once again, transferring the shares in favour of the purchaser. But in the case of a blank transfer the buyer can either fill in his own name on the transfer form or resell the shares by handing over the blank transfer form along with the share certificate to the new purchaser, who can again insert his name as the transferee or pass on the blank transfer form along

with the share certificate to another, and so on. Thus the same transfer form is instrumental in bringing about several buying and selling transactions till the share certificate and the transfer form come to the hands of a purchaser who wishes to retain the shares.

Possession of share certificate with blank transfer constitutes a good title to the shares. But shares are goods within the meaning of the Indian Contract Act and the Indian Sale of Goods Act, and therefore if a person obtains, by fraud, possession of a share certificate and a blank transfer executed by the owner, he cannot pass a good title even to a bonafide purchaser for value.

✓ **Forged Transfer.** A forged transfer is absolutely void as against the registered holder of the shares who can compel the company to replace his name on the Register of Members in respect of all the shares mentioned in such transfer, if it has been acted on by the company. Further, the company is liable in damages to any person who has acted in good faith on a certificate issued by the company on the strength of a forged transfer. It is very essential, therefore, that the secretary should take every precaution to ascertain that the signatures on transfers are genuine, before actual registration has been completed.

The notices to transferors mentioned above give no absolute protection to the company in the matter, for the courts have held that a member does not forfeit his rights by failing to answer such a notice. It is, however, a considerable safeguard, and in conjunction with the checking of signatures where possible reduces to a minimum the risk of a forgery passing undetected.

Transmission of Shares. It has been stated above that a company cannot register a transfer of shares unless a proper instrument of transfer together with the share certificate is lodged with the company. Section 34 (G), however, provides that this provision shall not prejudice any power of the company to register as shareholder any person to whom the right to any shares in the company has been transmitted by operation of law, e.g., on account of the death or insolvency of a member.

Section 35 says that a transfer of the share or other interest of a deceased member of a company made by his legal representative shall, although the legal representative is not himself a member, be as valid as if he had been a member, at the time of the execution of the instrument of transfer. On the death of a member, therefore, the right to transfer the shares registered in his name is conferred by the statute on his legal representative.

Similarly by operation of law the right of transfer vests in the duly appointed receiver of an insolvent member.

The exact method by which those entitled to deal with the shares of a deceased or insolvent member can obtain legal title to such shares or exercise their right of transfer is usually prescribed by the company's articles. Regulation 22 of Table A, dealing with the transmission of shares, reads as follows:—

"Any person becoming entitled to a share in consequence of the death or insolvency of a member shall, upon such evidence as may from time to time be produced to the company, be entitled to the same as if he had been a member."

required by the directors, have the right, either to be registered as a member in respect of the share or, instead of being registered himself, to make such transfer of the share as the deceased or insolvent person could have made; but the directors shall, in either case, have the same right to decline or suspend registration as they would have had in the case of a transfer of the share by the deceased or insolvent person before the death or insolvency."

It means that any person becoming entitled to a share on account of the death or insolvency of a member can, upon such evidence being produced as the directors may require, either have himself registered as a member in respect of the share or transfer the share to someone else. The nature of evidence demanded by the directors would naturally depend upon the circumstances of each individual case.

A person to whom the shares are transmitted through operation of law is usually required to send to the company a letter of request accompanied by the share certificate and the necessary evidence of his title, before his name can be registered as a member in place of the deceased or insolvent person.

Statutory Books and Accounts

One of the most important duties of a company secretary is to see that the various books, which every company is required by law to keep, are properly kept. These books are as follows:—

1. ✓ Register of Members.

Every company is required by section 31 to keep a register of its members, which must contain the following particulars:—

1. ✓ The names, addresses, and occupation of the members of the company;
2. ✓ The number of shares held by each member and the distinctive numbers of such shares;
3. ✓ The amount paid or agreed to be considered as paid on the shares of each member;
4. ✓ The date at which each person was entered in the register as a member; and
5. ✓ The date at which any person ceased to be a member.

In case of joint holders of shares, the company has the right to determine whose name shall be entered first. Generally, the person whose name appears first in the register has the right to attend and vote at meetings of the company. Pursuant to section 32, the register of members must contain, in a separate part, a list of members and summary of capital which is prepared annually within 21 days after the date of the annual general meeting. No particular ruling is prescribed for this register.

The register of members is the creditors' guarantee showing them to whom and to what they have to trust and must consequently be properly kept, so that the names appearing there are all the names of the persons really for the time being liable to the creditors. The register of members is *prima facie* evidence of membership, but it is not conclusive evidence.

Index of Members. A company with more than fifty members must keep, under section 31-A, an index of the names of members and, within 14 days of any alteration, must make the necessary alteration in the index. The index may be in the form of a card index, but it must contain sufficient indication to enable the account of any particular member in the register to be readily found.

Inspection and Copies of the Register. Under section 36, the register of members and the index must be kept at the registered office of the company. Every member is entitled, free of charge, to inspect the register and the index and to make extracts therefrom, but an outsider can have this privilege only on payment of a fee not exceeding one rupee. Copies of the register or any part thereof may be demanded by any person, whether member or not, on payment of six annas for every hundred words or fraction thereof; and the company must send such copy to the applicant within ten days.

Rectification of Register. Section 38 provides a summary mode of rectifying the register from time to time by application to the court in two classes of cases, viz. —

(i) where the name of any person is fraudulently or without sufficient cause entered in or omitted from the register of members, or (ii) where default is made or unnecessary delay takes place in entering on the register the fact of any person having ceased to be a member.

The court may either refuse the application or may order rectification of the register.

No Trust to be entered on Register. According to section 33 no notice of any trust, express or implied or constructive, shall be entered on the register of members. This means that the persons whose names appear on the register as the holders of shares may be treated in all ways as the beneficial owners by the company. The register does not show and the company is not required to take note of the fact that any shares may be held in trust or subject to any other equitable interest.

British Register. A company having a share capital may, if so authorised by its articles, keep in the U. K. a branch register of members called a British Register. The British Register is deemed to be a part of the company's principal register of members and shall be kept in the same manner as the principal register. A copy of every entry made in the British Register must be transmitted to the company's registered office in India for being recorded in the duplicate of the British Register to be kept as part of the principal register.

The British Register is kept by companies having a large number of British shareholders so that such shareholders may have no inconvenience in regard to the transfers of their shares.

Closing the Register. A company may, under section 37, on giving seven days' previous notice by advertisement in some newspaper circulating in the district in which the registered office of the company is situate, close the register for any time or times not exceeding in the whole 45 days in each year, but not

exceeding 30 days at a time. The register has to be closed when dividend warrants are written up after the declaration of dividend, when the annual return is prepared, when further shares are offered to existing members pro rata, or when the share capital of the company is reconstructed.

2. Annual Return.

Under section 32, every company having a share capital shall within eighteen months from its incorporation and thereafter once at least in every year make a list of all persons who on the day of the first or only ordinary general meeting in the year are members of the company and of all persons who have ceased to be members since the date of the last return or incorporation of the company. The list must state the names, addresses and occupations of all past and present members and the number of shares held by each of the existing members, specifying shares transferred since the date of the last return or incorporation and the dates of registration of the transfers.

The list must contain also a summary distinguishing shares issued for cash and those issued for any other consideration, and must specify the following particulars —

1. The amount of the share capital and the number of shares into which it is divided ;
2. The number of shares taken from the commencement of the company up to the date of the return ;
3. The amount called up on each share ;
4. The total amount of calls received ;
5. The total amounts of calls unpaid ;
6. The total amount of commission in respect of shares or of debentures ;
7. The total number of shares forfeited ;
8. The total amount of shares or stock for which share warrants are outstanding ;
9. The total amount of share warrants issued and surrendered respectively since the date of the last return ,
10. The number of shares or amount of stock comprised in each share warrant ;
11. The names and addresses of directors, managers or managing agents and the changes in their personnel since the last return with the dates of the changes ; and
12. The total amount of debt due from the company in respect of all mortgages and charges required to be registered with the Registrar.

The above list and summary is known as the 'Annual Return.' It must be contained in a separate part of the *Register of Members* and must be completed within 21 days from the first or only ordinary general meeting in the year ; and a copy thereof, signed by a director, manager or secretary, with a certificate as to its correctness, must be filed with the Registrar.

A private company must also send with the annual return a certificate

5. Register of Contracts.

Under section 91-A, every company must keep a register of contracts in which the directors are directly or indirectly concerned or interested, and such a register shall be open to the inspection of all members of the company at the registered office of the company during business hours.

6. Register of Mortgages and Charges.

Every company, according to section 123, must keep a register of mortgages and charges and enter therein *all* mortgages and charges specifically affecting the company's property and all floating charges on the undertaking of the company, giving in each case a short description of the property mortgaged or charged, the amount of the mortgage or charge, and the names of mortgagees or persons entitled thereto except in the case of securities to bearer.

7. Register of Debenture-holders.

It is not legally compulsory to keep a register of debenture-holders, but if one is kept, as is always the case when debentures are issued, section 125 requires that it shall be open to the inspection of debenture-holders and shareholders, except when closed in accordance with the articles during periods specified in the articles—not exceeding 30 days in any year.

Every company must keep at its registered office a copy of every instrument requiring compulsory registration under section 103.

Copies of instruments kept by the company at its registered office under section 117 and the register of mortgages kept under section 123 must be open to inspection (at all reasonable times) of any creditor or member of the company without charge, and the register of mortgages must also be open to the inspection of any other person on payment of the prescribed fee not exceeding one rupee for each inspection.

8. Books of Account.

Section 130 provides that every company must keep proper books of account for recording (a) all sums of money received and paid by the company and the matters in respect of which the receipt and payment take place; (b) all purchases and sales of goods made by the company; and (c) all assets and liabilities of the company.

The law does not prescribe any particular system of book-keeping; nor does it lay down any particular language in which the accounts should be kept. The books of account may be kept according to the English system of accountancy or the Indian system of *Bahi Khata*; but the accounts kept must be complete.

The books of account are to be kept at the registered office or at such other place as the directors think fit.

Where a company has a branch office, proper books of account relating to the transactions effected at the branch may be kept at the branch office; but proper summarised returns, made up to dates at intervals of not more than two months, must be sent by the branch office to the head office for incorporation in the principal books of account.

sub.subsidiary company, and (ii) a statement showing how the aggregate profits and losses of the subsidiary companies have been dealt with in the accounts of the holding company.

Profit and Loss Account. The law relating to the contents of the profit and loss account is contained in Regulation 107 of Table A, which applies to all companies and in section 132 (3).

Regulation 107 of Table A provides as follows:—(a) The profit and loss account shall show, arranged under the most convenient heads, the amount of gross income, distinguishing the several sources from which it has been derived; (b) The profit and loss account shall show, arranged under the most convenient heads, the amount of gross expenditure distinguishing the expenses of the establishment, salaries and other like matters, (c) Every item of expenditure fairly chargeable against the year's income shall be brought into account, so that a just balance of profit and loss may be laid before the meeting; and (d) Where any expenditure has been incurred during the year, which may in fairness be distributed over several years, the whole amount of such expenditure must be stated in the profit and loss account together with the reason why only a portion thereof is charged against the income of the year, unless the company has decided otherwise in general meeting.

Section 132 (3) requires (i) that the directors' remuneration, the managing agents' remuneration and the amount of depreciation shall be shown as separate items in the profit and loss account, and (ii) where any director is nominated by a company as a director of some other company, any remuneration received by such director from that other company must be shown in the profit and loss account of the company as a footnote or in a statement attached thereto.

Common Seal

A company is a *legal persona*, i.e., a separate entity entirely distinct from the members composing it. It is, therefore, necessary that all contracts, letters and other documents requiring the company's signature must be signed in such a way as to indicate clearly that the signature is the act of the company. In accordance with section 73, every company is required to have a common seal upon which the company's registered name must be engraven in legible characters. The law requires the name of the company to be 'engraven' on the common seal. Therefore a rubber stamp cannot serve the purpose of a common seal.

The common seal acts as the official signature of the company. The articles invariably contain provisions governing its use. Regulation 76 of Table A, for example, provides that the seal shall not be affixed to any instrument except by the authority of a resolution of the Board of Directors, and in the presence of at least two directors and of the secretary or such other person as the directors may appoint for the purpose, and these two directors and secretary or other person as aforesaid shall sign every instrument to which the seal is so affixed in their presence.

A company is not required to affix its seal to every document. Only those

documents need be sealed, for which sealing is made compulsory by the Act or by the company's articles, such as share certificates, share warrants, debentures, and important contracts. Other instruments made on behalf of the company are signed by the directors and are not sealed.

The custody of the keys of the seal is a matter usually provided for by the directors.

A seal book should be kept for recording particulars of all documents to which the seal of the company is affixed. A brief description of the document sealed, together with the date of the directors' resolution authorising the sealing, and the names of the persons who signed the document and witnessed the affixing of the seal, should be noted in the seal book.

Company Resolutions

There are four kinds of resolutions used by companies working under the Indian Companies Act of 1913, and these are as follows:—

1. *Ordinary Resolution.* Such a resolution is one which is passed by a simple majority in person or, where proxies are allowed, by proxy, in other words, a bare majority of those present who are entitled to vote and who do vote by a show of hands, poll or ballot. The Act does not define an ordinary resolution, but indirectly it is referred to as 'a resolution passed by a company in general meeting.' It is the kind of resolution used for ordinary routine business at general meetings. It can also be used for special business, e.g., alteration of capital under section 50, unless the Act or the articles of the company demand an extraordinary or special resolution.

2. *Extraordinary Resolution.* Section 81 (1) defines an extraordinary resolution as one passed by a majority of not less than three-fourths of such members entitled to vote as are present in person or by proxy (where proxies are allowed) at a general meeting of which notice specifying the intention to propose the resolution as an extraordinary resolution has been duly given.

An extraordinary resolution is necessary to carry out any of the following:—

- (a) To remove a director whose period of office is liable to determination at any time by retirement of directors in rotation (Section 86-G)
- (b) To institute a voluntary winding up on the ground of insolvency (Section 208).
- (c) To enable the liquidator to make compromises or arrangements with creditors (Sec. 212).
- (d) To carry out any specified purpose provided for in the articles of the company.

3. *Special Resolution.* Section 81 (2) defines a special resolution as one passed by such a majority as is required for the passing of an extraordinary resolution and at a general meeting of which not less than twenty-one days' notice, specifying the intention to propose a resolution as a special resolution, has been duly given.

The only difference between a special and an extraordinary resolution is

the *length of notice*, but if all the members who are entitled to vote be present and agree, then a special resolution may be passed at *less notice* than twenty-one days

A special resolution is required to carry out any of the following :—

- (a) To change the name of the company (Section 11).
- (b) To transfer the registered office of a company from one province to another or to alter its objects (Section 12).
- (c) To alter the articles of association of a company (Section 20).
- (d) To reduce the share capital of the company (Section 55).
- (e) To create reserve liability (Section 69).
- (f) To alter the memorandum so as to make the liability of a director unlimited (Section 71).
- (g) To sanction the assignment of office by a director (Section 86.B).
- (h) To sanction additional remuneration of managing agents (Section 87.C).
- (i) To appoint inspectors to investigate the affairs of the company (Section 142).
- (j) To initiate a winding up by the Court (Section 162).
- (k) To wind up a company voluntarily (Section 203).
- (l) To confer authority on the liquidator in a voluntary winding up to enter into any arrangement with a transferee company (Section 209.C).

Where articles have been registered, a copy of every special resolution for the time being in force shall be embodied in or annexed to every copy of the articles issued after the date of the resolution. Where articles have not been registered, a copy of every special resolution shall be forwarded in print to any member at his request, on payment of one rupee or such less sum as the company may direct.

Note.—The following matters are common to both extraordinary and special resolutions :—

1. The meeting must be properly convened, but if all the shareholders are present and agree, any informality may be waived.
2. The meeting must be properly constituted, the chairman duly appointed, and a quorum present.
3. The requisite majorities must consist of persons entitled to vote. The articles may prohibit members with calls in arrear.
4. The chairman's declaration that the resolution has been carried or lost is conclusive unless a poll is demanded.
5. A poll may be demanded by such number of members entitled to vote as are mentioned in section 79 (1) (c).
6. A printed or typewritten copy of every extraordinary and special resolution duly certified under the signature of an officer of the company must be filed with the Registrar within fifteen days of the passing of the resolution.
4. *Other Resolutions.* The fourth type of resolution is the one which

requires special majorities, e. g., as provided in section 153.

General Meetings

A meeting may be defined as the gathering together of two or more persons by previous notice or mutual arrangement for the discussion and transaction of some business. Meetings of members of companies are known as general meetings or company meetings. Although a joint stock company is managed by its directors, the ultimate control of the company is in the hands of its members (i. e., proprietors) collectively, and in order that it may be possible for them to exercise such control, certain machinery has been provided by the legislature. The machinery consists of rules and regulations for the holding of periodical meetings of the members of every company and the procedure and business relating to such meetings.

There are three kinds of general meetings provided by law, viz., Statutory Meeting, Ordinary General Meeting and Extraordinary General Meeting.

Who is a member A general meeting of a company is a meeting of its members. But who is a member? The term 'member' is carefully defined in section 30 by which two distinct things are necessary in order to make a person a member of a company, namely, (i) That person must have agreed to become a member of the company, and (ii) His name must be on the register of members.

A person agrees to become a member in three ways: In the first place, section 30 provides that every person who signs the memorandum of association shall be deemed to have consented to become a member, secondly, every applicant for an allotment of shares, whose offer is accepted before it has lapsed or been revoked, consents to become a member, and thirdly, every person who agrees to take a transfer of shares from a member consents to become a member.

The latter requirement is just as important as the former. A person who agrees to become a member does not become a member until his name is put on the register of members.

The term 'shareholder' does not possess the same meaning as the term member. The person who holds a share warrant payable to bearer is a shareholder. But he is not a member because his name does not appear on the register of members. Again the legal representative of a deceased or insolvent member is not a member until he applies to the company for registration as a member, although he is a shareholder even without being placed on the register of members. The term member does not necessarily include every shareholder. Moreover, in the case of guarantee companies not having share capital, it includes people who hold no shares at all.

1. Statutory Meeting.

Section 77 provides that every public company limited by shares and every public company limited by guarantee and having a share capital shall, within a period of not less than one month nor more than six months from the date on which it is allowed to commence business, hold a general meeting of its members.

This meeting is called the *statutory meeting*. The statutory meeting is usually the first meeting of the company, but it is possible, though it would be unusual, that, as this meeting can be held within six months from the date the company is entitled to commence business, the first annual general meeting of the company which is required to be held within 18 months from the date of its incorporation, may be the first meeting.

The object of the statutory meeting is to give shareholders an opportunity of learning, at an early stage in the company's career, details of the formation of the company, to what extent the financial appeal to the public has been successful, what property has been acquired by the company in exchange for its subscribed capital, and what has been done with the actual money received in payment of shares. It enables shareholders to discuss these and any other matters arising therefrom, and to approve the modification of the terms of any contract disclosed in the prospectus.

A list of members showing names, addresses and descriptions must be available for the inspection of members during the continuance of the meeting. The members present at the meeting can freely discuss any matter relating to the formation of the company or arising out of the statutory report, and, if any resolution for which the articles require a specific notice to be given is proposed, the meeting can be adjourned to enable such notice to be given.

Statutory Report. The directors shall, at least 21 days before the day on which the statutory meeting is to be held, forward a report (called the Statutory Report) to every member of the company. The report should furnish prescribed particulars regarding shares allotted, money received on account of such shares, receipts and payments of the company, preliminary expenses, directors and other officers of the company, contracts, if any, which are to be modified, arrears, due on calls from directors, etc., commission and brokerage paid on shares. The report must be certified by at least two directors or by the chairman if so authorised by the directors; and certain particulars contained therein must also be certified by the company's auditors.

The directors must cause a copy of the statutory report to be filed with the Registrar forthwith after the sending thereof to the members of the company.

Below is given the prescribed form of the statutory report :—

Statutory Report
THE INDIAN COMPANIES ACT, 1913

[Sec. Section 77].

Filing fee Rs. 3

Name of Company.....
Statutory Report of the..... Limited,
certified and filed pursuant to section 77 (5).
Date and place of the statutory meeting.....
Presented for filing by.....
The Directors report to the members as follows :—

1. Shares allotted up to ... day of ... 1st (i.e. a date within 7 days of the report) and cash received up to the aforesaid date were :—

Particulars	Number of Shares.	Nominal Value of each share	Cash Received.
(a) Allotted subject to payment therefor in cash	Preference* Ordinary Deferred		
(b) Allotted as fully paid up otherwise than in cash, the consideration for which they have been so allotted being :	Preference* Ordinary Deferred		Nil Nil Nil
(c) Allotted as partly paid up to the extent of Rs. ... per share, the consideration for which they have been so allotted being :—	Preference* Ordinary Deferred		
(d) Allotted at a discount of Rs. ... per share	Preference* Ordinary Deferred		
... ..	Total		

*Redeemable Preference Shares are to be specified in all cases.

2. The receipts and payment of the Company up to the aforesaid date are as follows :

Receipts	Rs.	Payments	Rs.
Shares—		Preliminary Expenses	...
Preference	Commission on Sale of Shares	...
Ordinary	Discount on Shares ...	...
Deferred	Capital Expenditure—	...
Share Deposits	Land ...	...
Debentures	Buildings ...	...
Loans	Plant ...	...
Deposits	Machinery ...	...
Other Sources (to be specified)	Dead Stock ...	...
		Other Items (to be specified) ...	...
		Balances—	
		In hand ...	...
		At Banks ...	...
Total		Total	...

3. Preliminary Expenses : as estimated in the Prospectus* or Statement in lieu of Prospectus Rs. ...

Preliminary Expenses incurred up to the aforesaid date :

Law Charges
Printing
Registration
Advertisement
Commission on sale of shares
Discount on shares
Other initial expenses

Total Rs.

*Strike out the portion which does not apply.

4. Names, addresses and descriptions of the Directors, Auditors (if any), Managing Agents and Managers (if any) and Secretary of the Company and the changes, if any, which have occurred since the date of the incorporation :—

Directors

Name	Address	Description	Particulars of changes, if any**

Auditors

Name	Address	Description	Particulars of changes, if any**

**These particulars must include dates of changes.

Managing Agents and Managers

Name	Address	Description	Particulars of changes, if any**

Secretary

Name	Address	Description	Particulars of changes, if any**

**These particulars must include dates of changes.

5. Particulars of any contract the modification of which is to be submitted to the meeting for its approval together with the particulars of the modification or proposed modification.

6. The extent to which underwriting contracts, if any, have been carried out.

7. The arrears, if any, due on calls from directors, managing agents and managers.

8. The particulars of any commission or brokerage paid or to be paid in connection with the issue or sale of shares to any director, managing agent, or manager, or if the managing agent is a firm, to any partner thereof, or, if the managing agent is a private company, to any director thereof.

Dated this .. day of .., 19.....

We hereby certify this report*

Two or more Directors,

(Alternatively)

I hereby certify this report

Chairman of the directors,

(If authorised by the Board of Directors)

We hereby certify that so much of the report as relates to the shares allotted by the Company and the cash received in respect of such shares and to the receipts and payments of the Company is correct.

Dated this day of 19

Auditors.

Note.—1. Receipts and payments account given in para (3) of the Statutory Report with reference to section 77 (3) (c) of the Indian Companies Act should be prepared up to a date within 7 days of the date of the report and the figures and particulars required under all the other items of the Statutory Report should also be given as on the same date, i. e., the date up to which the receipts and payments account is prepared.

2. This form should contain the actual signatures of the persons who have signed the report, viz., the Directors or the Chairman and the Auditor.

*To be certified by not less than two Directors or if the Company has less than two Directors, by the sole Director, and forwarded at least twenty-one days before the statutory meeting to every member and debenture-holder of the Company and to be filed with the Registrar forthwith after it is forwarded, vide Section 77 (2), (3) and (5), and section 146.

Secretary's Duties. The secretary's duties in connection with the statutory meeting may be summarised as follows:—

1. When the date of the statutory meeting has been fixed by the directors, he will prepare the statutory report in the prescribed form, get it audited by the company's auditors, and have sufficient copies thereof printed.

2. A copy of the statutory report duly certified by directors and auditors will be sent, along with the notice of the meeting, to every member of the company at least 21 days before the date of the meeting. The notice must specify the nature of business to be done at the meeting.

3. Immediately after the report has been sent to members, a copy must be filed with the Registrar.

4. He should prepare a list showing the names, addresses and descriptions of members of the company, and the number of shares held by them respectively. The list to be open to inspection of any member during the continuance of the meeting.

5. At the meeting the secretary would read the notice convening the meeting and exhibit the list of members for inspection.

6. During the progress of the meeting, he must take notes of the proceedings, from which he will afterwards write up the minutes.

7. After the meeting, he must prepare the minutes of proceedings and give effect to any resolutions passed.

2. Ordinary General Meeting

Section 76 makes provision for the holding of ordinary general meetings of a company. A general meeting of every company shall be held within eighteen months from the date of its incorporation and thereafter once at least in every calendar year (i.e., between 1st January and 31st December) so that the interval between any two successive ordinary general meetings is not more than fifteen months. These meetings are called ordinary general meetings or annual general meetings. In India many companies, however, hold half-yearly ordinary general meetings.

The business to be transacted at an ordinary general meeting is either only ordinary business or both ordinary and special business. The ordinary business consists of the consideration of the company's audited accounts, declaration of dividend, election of directors and appointment of auditors. All other business that may be transacted at a company meeting is classed as special business. An ordinary general meeting is held mainly for the purpose of doing the ordinary business; but if the articles so permit, any special business may also be done at an ordinary general meeting. Otherwise all special business has to be transacted at what are known as extraordinary general meetings of the company.

Annual Accounts. The directors of every company are required by section 131 (1) to lay before a general meeting of members in each calendar year an audited balance sheet and an audited profit and loss account together with the auditor's report. The first accounts must be presented at some date not later than eighteen months after the incorporation of the company, and subsequent accounts must be presented once at least in every calendar year. Many companies in India prepare half-yearly accounts and hold half-yearly ordinary general meetings.

Under section 131 (3), every company, other than a private company, is required to send a copy of the audited accounts together with a copy of the auditors' report to every member at his registered address, at least fourteen days before the meeting at which they are to be presented. The period of 14 days is intended to give the members an adequate opportunity for considering the accounts.

Directors' Report. Under section 131.1, a Directors' Report dealing with the following matters must be attached to every balance sheet :—

- (a) The state of the company's affairs ; and
- (b) The disposal of the company's profits, namely—(i) The amount which the directors recommend by way of dividend, and (ii) The amount which the directors propose to carry to reserves shown specifically on balance sheet to which the report is attached or to be shown in a subsequent balance sheet.

It is to be signed by the same persons as are required to sign the balance sheet ; but it may be signed by the chairman alone if so authorised by the directors. In this respect it stands on the same footing as the statutory report.

The object of the directors' report is to enable the shareholders to know something about the company's progress and the manner in which its profits are being dealt with. If the directors report, instead of being confined merely to minimum requirements of law, is carefully drafted so as to review the accounts and explain their salient features, it will prove a very useful document.

The directors report is usually drafted by the secretary, but the information to be disclosed therein is settled by the directors. The following are actual specimens of directors' reports :—

1. The Standard Coal Company, Limited

Directors' Report

To

The Shareholders

Gentlemen,

We beg to submit the audited accounts for the half-year ended 31st December 1940.

Raisings and Despatches.—96,016 tons were raised and 100,374 tons despatched during the half-year, as against 112,594 tons raised and 107,763 tons despatched during the previous half-year.

Despatches to the Indian Iron and Steel Company, Limited, were made in full throughout the half-year.

Sand-Stowing.—Work is proceeding in connection with the erection of the Ropeway for the transport of sand from the Damodar River to the Colliery. It had been hoped to have this Ropeway in operation by December 1940, but owing to unforeseen delays due to war conditions, it is now unlikely that the Ropeway will be working before the end of 1941.

It must also be mentioned that a considerable amount of consolidation work will need to be done before the introduction of sand-stowing can lead to increased output. The continuation of the present reduced level of output must, therefore, be expected to continue during 1941, and for some months thereafter. Further, more mining difficulties being met in areas now in process of development may lead to further reductions in output.

Market.—The market remained quiet throughout the half-year with a

tendency to a fall in prices during the end of the period. The outlook for the coal industry owing to surplus production and shortage of freight is most unsettled.

Colliery.—The mines and machinery were maintained in good order.

Accounts.—Owing to the recent increase in the surcharge on Income Tax it has proved necessary to provide in this year's accounts for additional taxation payable in respect of previous half-year's profits.

The Profit and Loss Account, after making provision for taxation, providing Rs. 23,187-0-6 for Depreciation, writing off Rs. 2,500 from Prospecting and including the sum of Rs. 7,362-14-3 brought forward from last half-year, shows an available balance of Rs. 44,605-10-1, which we propose to dispose of as follows :—

			Rs.	A.	P.
In paying a Dividend at the rate of 10 per cent per annum, free of Income Tax	...	...	40,000	0	0
In carrying forward	...	...	4,605	10	1
		...	44,605	10	1

Directorate.—Mr. D. H. Wilmer retires at this time, and, being eligible, offers himself for re-election.

Auditors.—Messrs. Price Waterhouse Peat and Company, Chartered Accountants, the Auditors of the Company, retire but offer their services for the ensuing year.

We are, Gentlemen,

Your obedient servants,

A. P. BENTHALL,
C. H. HEAPE,
A. C. BANERJEE,
D. H. WILMER,

} *Directors.*

McLeod House,

28, Dalhousie Square,

Calcutta, 15th July, 1947.

To

The Shareholders,

The Eastern Manufacturing

Company, Limited.

Gentlemen,

We beg to submit our Report and Audited Statement of Accounts for the year ended 31st December, 1946.

Profit and Loss Account.—including the balance brought forward from last year and after charging Interest, Commission, etc., writing off Rs. 32,287 for Depreciation, and making provision for Taxation shows a credit balance of Rs. 1,42,461-3-7 which we recommend should be dealt with as follows :—

Pay the dividend due on the Rs. 2,00,000 @ per cent.	Rs.	A.	P.
Cumulative Preference Shares for the year ended 31st December, 1946	...	...	12,000 0 0

• Pay a dividend on the Rs. 8,50,000 Ordinary Shares at the rate of 10 per cent. per annum or Rs. 10 per share for the year ended 31st December, 1946	...	85,000	0	0
Transfer to Reserve Account	...	25,000	0	0
Carried forward to Profit and Loss Account	...	20,461	3	7
Total Rs.	...	1,42,461	3	7

Jute Stocks are shown at or under cost price. Stocks of sold and unsold Webbing and Sashcord have been calculated at or below market prices. Unfinished goods have been taken at cost price.

Buildings, Power Plant and Machinery have been maintained in thorough repair.

The factory continued to work double shift during the year with the exception of the Sashcord Department which worked single shift. With the introduction of the Factories (Amendment) Act, 1946, working hours were reduced to 48 hours per week and our double shift working was therefore automatically reduced to 96 hours per week. Workers received the same wages for 48 hours working as they previously did for 54 hours.

Webbing continued to be in considerable demand particularly in the U. K. and U. S. A. markets. Experiments are being carried out in an endeavour to obtain dyes of good light fastness on Jute for resumption of production of carpet material. These experiments are proceeding satisfactorily.

Board of Directors.—Mr. H. N. Thomas resigned his seat on the Board and Mr. W. L. Elliot was appointed by the Board to fill the vacancy. Mr. G. S. Johnston has since been appointed to fill the vacancy on the Board in place of Mr. W. R. Elliot resigned.

Messrs. Chhotaylal Kacoria and G. S. Johnston retire by rotation and, being eligible, offer themselves for re-election.

Auditors.—Messrs. Lovelock & Lewis retire but seek reappointment.

We are, Gentlemen,

Yours faithfully,

_____ } *Directors.*

Chairman's Speech. At ordinary general meetings of companies, it is the usual practice for the chairman to make a speech in placing the audited accounts and the directors' report before the members for their consideration and approval. It is not legally-necessary that the chairman should do so, but this is always done. A printed copy of the chairman's speech is usually made available for the information of those interested in the company. In recent years many companies have adopted the practice of publishing their chairman's statement or review simultaneously with the annual accounts.

The chairman's speech or statement has a special value. It is a picture of

the industry in which the company is engaged, drawn by one who has a stake in it and who is in touch with it, day in and day out. When a chairman speaks at the annual meeting, he is addressing not the shareholders alone, but the country as a whole. The speech, therefore, calls for and fully deserves the utmost publicity. That is why so many chairman's speeches appear from time to time in financial journals.

What the present and prospective shareholders of a company desire to know from the chairman's speech is news about the company, its achievements, its aims, its hopes and its problems. Investors, indeed, have an appetite for positive facts, from which they can draw their own conclusions with the assurance that no consideration which is basic to their decision has been omitted. The best speech can never be a satisfactory substitute for detailed and informative annual accounts. Its ultimate function, indeed, is to give these annual figures their due perspective, to remove misapprehensions, and to elucidate the causes which have brought them about. There is obvious utility in a speech which specifies the directions in which a company's business is expanding, the new products it is manufacturing and the new branches it is about to open. Equally useful is the speech which describes the background of the industry in which the company is a single unit. Whether an address which amply covers all these points can leave any room for controversial propaganda is perhaps an open question. A certain seeing of facts through rose coloured spectacles may be permissible, if shareholders and investors can determine the tint employed more or less accurately. On the whole they have reason to complain of speeches which tell them too little rather than too much.

The secretary has, in many cases, to draft the chairman's statement or review. The matter to be included in it will, of course, be decided in consultation with the chairman. The following is an actual chairman's speech:—

The Ahmedabad Advance Mills. Limited.

Speech delivered by the chairman, Sir Sorab Saklatvala Kt., at the annual general meeting of the shareholders of the company on Tuesday, the 25th October 1947.

Gentlemen,

Before dealing with the business of this meeting I would like to refer to the most outstanding event of the year—the attainment of independence by India. It is indeed a unique event in world history that after years of struggle India has achieved her freedom from foreign rule without bloodshed. We pay our tribute to our national leaders who strived for years, patiently and non-violently, for India's freedom. However, a great deal remains to be done for the country's economic recovery. Unfortunately, the disturbances that occurred recently in some parts of India have disorganised the trade of the country. During the last year frequent labour strikes also proved to be the most serious handicap to production in almost all the major industries of the country. It is deplorable that this should happen at a time when there is acute shortage of food, clothing,

raw materials and almost all other necessities of life, and the need for more production is imperative.

So far as your mill is concerned you must have noticed from the Directors' report the reasons that have contributed to the fall in production during the year. The reduction in mill working hours from 54 to 48 per week naturally caused a substantial reduction in production, but the closure of the mills during the riots in July 1946 and its after effects which lasted for several months, account for a further big drop. It was not till January 1947 that normal two-shift working was resumed. The result of this fall in production is clearly reflected in the accounts.

Mention has been made in your Directors' report about the proposed change in the source of power supply to the mills. I am glad to tell you that from the 6th of the current month the entire mill has been switched over to electric power supplied by The Ahmedabad Electricity Co. Ltd.

I shall now, as usual, briefly explain some of the important items in the accounts.

In the Balance Sheet, page 6, you will find Rs. 13,805 credited to the Reserve Fund. This is the surplus over cost realised from the sale of a chawl at Navsari. This chawl was built in 1926 as a working-class tenement. An offer of Rs. 42,051 was received for the chawl and the land appertaining to it. At the upkeep of the chawl and the rent realised were uneconomical, your Directors considered it advisable to dispose it of. The original cost of the chawl and the land *viz.* Rs. 28,246 has been written off against the assets, and the surplus of Rs. 13,805 has been credited to the Reserve Fund.

As regards the "Provision for Taxes" account page 8, you will observe that a sum of Rs. 7,50,000 has been provided for taxation for this year. This consists of Rs. 4,20,000 for Income-tax, Rs. 1,70,000 for Super-tax and Rs. 1,60,000 for Business Profits Tax.

The Company's "Deposits with Government against post-war refund of excess profits tax" amounted to Rs. 11,97,895 out of which Rs. 2,31,002 were received back in April last, leaving a balance of Rs. 9,66,893 as shown in the Balance Sheet on page 11. In addition to this sum, we shall be receiving in due course a sum of about Rs. 4,55,000 by way of refund of one-tenth of the excess profits tax. This will of course be subject to income-tax and super-tax.

Our "Investments", page 11, have decreased to the extent of the repayment of the Tata Mills' Preference shares, a reference to which has been made in the Directors' report.

Turning to the Profit and Loss Account you will observe that the majority of items both on the credit and the debit sides show a considerable decline compared to the previous year. This is mainly due to the fact that production was low for the reasons I have already stated.

The Company's contribution to the Provident Fund shows a substantial increase. Realising the benefits of the provident fund more workers are now

becoming members. The total number of contributors which was 536 last year rose to 1,174 during the year under report.

Gentlemen, I now move that the Directors' Report and Audited Statements of Accounts for the year ended 30th June 1947 already circulated among shareholders be adopted.

Secretary's Duties. As an ordinary general meeting of a company is an annual affair, the secretary has to do a good deal of work in connection with it. His duties are as follows ;—

1. When the company's accounts have been audited and the auditor's report received, they will be considered by the directors who will decide how the profits are to be appropriated. The secretary will then prepare the Director's Report and have it approved and signed by them. The directors will also fix the date of the meeting and the time for which the share books of the company are to be closed.

2. The secretary should arrange for the printing of the audited accounts, auditors' report, directors' report and the notice of the meeting. All these are usually printed together in the form of a booklet.

3. The notice and the annual accounts must be sent, at least fourteen days before the date of the meeting, to every member and also to those other persons who, under section 146, are entitled to receive them. These other persons are debentureholders and debenture trustees. A copy of the accounts must also be deposited at the registered office of the company for the inspection of the members during a period of at least 14 days before the meeting. For the sake of foreign shareholders, a copy of the notice convening the meeting must be advertised in some newspapers and must also be put up on a notice board at the registered office of the company.

4. The share transfer books of the company are closed for the purpose of balancing the Register of Members, writing up dividend lists and dividend warrants, and preparing the Annual Return. The general practice is to close the books for a period (usually fourteen days) expiring on the day appointed for the holding of the annual meeting. This fixes definitely the names of those members entitled to receive dividends, as there can be no change in membership during the time the dividend warrants are being prepared, because the registration of transfers will be suspended for this period. On the first day of the closed period the secretary should immediately deal with any transfers awaiting registration, and proceed with the balancing of the Register of Members in order to ascertain the names of those members to whom dividends are to be paid and whose names will appear in the Annual Return.

5. If the articles allow the use of proxies, as they usually do, arrangements must be made for dealing with any proxies lodged with the company. Proxies must be scrutinised to ascertain that they are in order.

6. Where it is anticipated that a poll may be demanded at the meeting, preparation should be made for polling.

7. A detailed agenda setting forth every step in the conduct of the meeting should be prepared. It will include the motions to be proposed, and the names of those members with whom arrangements have been made to propose and second the motions.

8. At the meeting the secretary will read the notice convening the meeting unless this is taken as read. During the progress of the meeting, he should take notes of the proceedings, and record verbatim the terms of all resolutions passed from which he will afterwards write the minutes.

9. When the meeting is over, he should prepare the minutes of proceedings and should take the necessary steps to give effect to the various resolutions passed at the meeting, such as the payment of dividend, informing the persons elected as directors and auditors, etc.

10. After the audited accounts have been laid before the ordinary general meeting, three copies thereof signed by the secretary must be filed with the Registrar. If the accounts have not been adopted by the meeting, a statement of that fact and of the reasons therefor must be annexed to the accounts.

11. The annual return must be completed within 21 days from the date of the meeting, signed by the secretary and filed with the Registrar.

3. Extraordinary General Meeting

All company meetings other than the statutory meeting and the ordinary general meeting are termed extraordinary general meetings. They are convened for conducting some special business, the nature of which is clearly indicated in the notice of the meeting. The need for holding an extraordinary general meeting may arise in this way. Suppose there is some special business to be done at a company meeting. If, according to the articles, such business cannot be transacted at an ordinary general meeting, or, if it can be done at an ordinary general meeting, it is of so urgent a nature that it cannot conveniently wait till the next ordinary general meeting, then an extraordinary general meeting must be held for doing it. Sometimes a company calls both the ordinary general meeting and the extraordinary general meeting to be held on the same date, one after the other, and in that case only one notice is issued to the members for both meetings. Extraordinary general meetings may be called in three ways:—

1. By the directors on their own initiative in accordance with the articles, whenever an extraordinary general meeting is deemed to be necessary;

2. By the directors upon shareholders' requisition mentioning the object of the meeting as provided in section 79, if the requisitioning shareholders hold not less than one-tenth of the issued capital on which there are no calls in arrear. On receipt of a shareholders' requisition, it becomes the duty of the directors to cause a meeting to be convened within 21 days,

3. By the requisitionists (members) themselves, if the directors fail to comply with the requisition within 21 days. The requisitionists can do so within three months from the date of the deposit of their requisition, and they will be entitled to recover any reasonable expenses incurred in calling the meeting.

from the company, which in its turn can claim the same from the defaulting directors.

The special business to be transacted at an extraordinary general meeting often requires an extraordinary or a special resolution of the company. Therefore the legal requirements relating to such resolutions must be duly complied with.

Special Circulars. As the business to be done at an extraordinary general meeting is in many cases of an important nature, it is usual to prepare a circular explaining in detail the nature of the special business, and send it along with the notice to the members, so that they may know beforehand why the meeting is being called and may decide whether or not to attend the meeting. The drafting of such circulars is another important duty of the secretary. Of course, the contents of the circular are decided in consultation with the directors. The following are specimen circulars :—

(1)

The Member,

. Co., Ltd.,

Dear Sir/Madam,

We are directed to inform you that the Directors of this Company have had under their consideration the desirability of bringing the Company's capital into harmony with its producing capacity.

The present authorised capital of the Company is Rs. 24,00,000 divided into 24,000 shares of Rs. 100 each, all of which are issued and fully paid : while the Company's Block Account (after deduction of depreciation) exceeds Rs. 30,00,000. The amount at the credit of the Reserve Fund is over Rs. 10,00,000 ; and it is proposed to capitalise Rs. 6,00,000 of this amount by the issue of fully-paid Ordinary Shares to the shareholders in the proportion of one new share for each four shares held. This will leave an amount of more than Rs. 4,00,000 at the credit of the Reserve Fund.

To enable these proposals to be carried into effect, the Directors ask the shareholders' sanction to increase the Company's authorised capital to Rs. 30,00,000. A notice is enclosed convening an Extraordinary General Meeting of the Company, at which resolutions approving and sanctioning the increase of capital, the capitalisation of reserve and the issue of bonus shares will be submitted.

A form of proxy is enclosed, which may be signed and returned to the Company immediately if you are unable to attend the meeting.

Yours faithfully,

.
Managing Agents,

(2)

The Burrakur Coal Company, Ltd.

To the Shareholders,

The Burrakur Coal Company, Ltd.

Dear Sir/Madam,

In recent Reports to Shareholders your Directors have referred to the installation of a Ropeway for the supply of sand for stowing purposes to certain of the Company's Collieries. An adequate and continuous supply of sand for stowing is now essential for the security and maintenance of these Collieries. The cost of this complete scheme is estimated to amount to approximately Rs. 50 lakhs, but it is intended to carry it through in several stages. While it is anticipated that with the help of the special depreciation allowances, a considerable proportion of the cost will be met out of reserves which it should be possible to conserve in the Company, it is calculated that some fresh capital will require to be raised.

To enable this to be done your Directors have given serious consideration to the Company's present capital structure. The authorized capital of the Company is Rs. 1,00,00,000 divided into 5,00,000 Ordinary Shares of Rs. 10 each and 50,000 7 per cent. Preference Shares of Rs. 100 each. Of the 7 per cent. Preference Shares 22,998 have been issued and your Directors recommend that 25,000 of the balance available for issue be cancelled and in lieu thereof 2,50,000 new 6 per cent. taxable Second Cumulative Preference Shares of Rs. 10 each be created. In making this recommendation your Directors would draw your attention to the present tendency towards cheaper money an example of which is the Government of India's recent decision to repay all outstanding $2\frac{1}{2}$ per cent. non-terminable loans with the option to holders to convert into 3 per cent. and $2\frac{1}{2}$ per cent. loans.

The proposals made by your Directors would effect a considerable saving to the Company as and when the new 6 per cent. Second Cumulative Preference Shares are issued—but at the same time ensure a fair return to investors. The proposed new shares would rank immediately after the existing Preference Shares and in priority to the Ordinary Shares in the Company both as regards payment of dividend and, in a winding up, as regards payment off of capital and arrears of dividend, whether declared or not up to the commencement of the winding up, but would not confer any further right to participate in profits or assets nor confer any voting rights.

If the above proposals meet with your approval your Directors further recommend that for the present 45,000 new 6 per cent. Second Cumulative Preference Shares be issued at a premium of Rs. 1 each and be offered in the first instance at such premium to the existing shareholders in the proportion of one new Second Cumulative Preference Share for every ten existing shares, whether Preference or Ordinary, held by them, fractions below one half being disregarded and one half and over being taken as one. It has been possible to make this offer to the shareholders in the proportion given above as certain

notice addressed to him and advertised in a newspaper circulating in the neighbourhood of the registered office of the company shall be deemed to be duly given to him on the day on which the advertisement appears.

According to regulation 116 of Table A, notice of every general meeting must be given to every member of the company (including bearers of share warrants) except those members who (having no registered address in British India) have not supplied to the company an address within British India for the giving of notices to them. Notice must also be given to every person entitled to a share owing to the death or insolvency of a member. It means that notice of a general meeting is to be given not only to every member but also to certain non-members such as the bearers of share warrants and the legal representatives of a deceased or an insolvent member.

Although all members and some non-members have a right to receive notice of a company's general meeting, yet they all do not enjoy the right to attend, speak or vote at that meeting. Of course, no non-members are allowed this privilege; but the articles of most companies also impose restrictions on the members themselves in respect of the right to attend, speak or vote at general meetings, *e. g.*, no member is entitled to be present or vote on any question either in person or by proxy or as proxy for another whilst any call or other sum shall be due and payable to the company in respect of any of the shares of such member.

Agenda

The term agenda means a statement of the business to be discussed and transacted at a meeting, and the order in which such business is to be dealt with. The preparation of the agenda is a necessary preliminary to the holding of a successful meeting. It is drawn up by the secretary in consultation with the chairman.

Proxies

A proxy is a person who is authorised to attend and vote at a company meeting on behalf of another person. The term is, however, more generally used for the document by which the person is authorised to act. At common law, there is no right to vote by proxy; but the articles of most companies contain regulations providing for and governing the use and form of proxy. The provisions of the articles must be strictly followed. Usually the person appointed to act as proxy must also be a member of the company.

Proxies must be in writing, properly stamped and signed by the shareholder. Although not classed as such, a proxy form is really a simplified power of attorney. The form of proxy is given in the articles of a company; but an instrument appointing a proxy, if in the form set out in regulation 67 of Table A (and given below) shall not be questioned on the ground that it fails to comply with any special requirements specified for such instruments in the articles:—

.....Company, Limited

I.....of.....in the district of.....being a member
of the.....Company, Limited, hereby appoint.....of.....

as my proxy to vote for me and on my behalf at the (ordinary or extraordinary, as the case may be) general meeting of the company to be held on the..... day of.....and at any adjournment thereof.

Signed this..... day of.....

Section 80 provides that a company, which is a member of another company may, by resolution of the directors, authorise any of its officials or any other person to act as its representative at any meeting of that other company, and the person so authorised shall be entitled to exercise the same powers on behalf of the company which he represents as if he were an individual shareholder of that other company.

Regulation 66 of Table A, which is compulsory for all companies, requires that proxy forms must be deposited at the registered office of the company not less than seventy-two hours before the time for holding the meeting at which the person named in the proxy form proposes to vote, and in default the instrument of proxy shall not be treated as valid.

All proxies lodged at the company's office must be carefully examined by the secretary in order to ascertain that the document was received at least 72 hours before the time of the meeting, that it is in proper form and stamped, that it is properly signed, that the name of the member agrees with the Register of Members, and that the person appointed is a member of the company (where this is required by the articles). The last point would not, however, apply to the representative of a company shareholder, as such representative need not himself be a member of the company.

Whether a proxy form is in order or not will be decided by the chairman of the meeting, but the secretary is expected to draw the chairman's attention to any forms which ought to be rejected. A list giving the names of the members who have appointed proxies, the number of votes to which they are entitled and the names of the persons appointed should be available for the use of the chairman.

Note.—The directors may, provided that they are acting *bona fide* in the interests of the company, utilise the company's funds in issuing, stamping, and obtaining proxies in their own favour. Owing to the apathy of the average shareholder and his unwillingness to attend company meetings, an appeal for proxy forms is frequently made by directors when seeking to carry through some scheme requiring the approval of members. The secretary is, therefore, sometimes required to send out, with the notice of meeting, stamped proxy forms and an invitation to shareholders to appoint one of the directors to vote at the meeting on their behalf.

Poll

Voting at company meetings is usually carried out in the same manner as at any other kind of public meeting, namely, by show of hands on the principle of 'one man, one vote.' Sometimes, however it becomes necessary that the

members of a company should be able to exercise voting power in proportion to their interest in the company, and in order to do so, voting is done by means of what is known as a 'Poll'. Voting by poll means a counting of all actual available votes as distinguished from a mere counting of votes on a show of hands. On a show of hands, each person counts as one vote, even though he may hold proxies for others. On a poll, votes are calculated according to the number of members present and the proxies held by them from members who are absent and also according to the number of shares held. A poll is usually resorted to when some important business is before the meeting for decision.

Who Can Demand a Poll. Members have the right under the common law to demand a poll on any motion before the meeting, but this right may be excluded or qualified by the articles. Under Section 79 (1), however, it is provided that five persons present in person or proxy or the chairman or any member holding not less than one-tenth of the issued capital which carries voting rights can demand a poll. In the case of a private company, one member or two members at least are required to demand a poll according as the members present in person at its meeting are either seven or more than seven.

How to Take a Poll. When a poll is duly demanded, the chairman must grant it and fix the time and place for taking it; for if a poll is duly demanded, the show of hands is nullified. If by the articles the poll is to be taken in such manner as the chairman directs, the poll may be taken then and there. The poll will be taken by every person who desires to vote, signing a paper headed, as the case may be, for or against the motion. The votes of each member are then inserted and these having been added up the chairman declares the result. The meeting or the chairman can appoint scrutineers to examine and count the votes at a poll and to report the result to the chairman.

On a poll being demanded, it may be taken at once if the necessary preparation has been made beforehand; otherwise the meeting may be adjourned for the purpose. Each member is supplied with a voting paper on which he says whether he is voting for or against, and mentions the number and class of shares held. If he is acting as a proxy he must name the member for whom he is acting. He then signs it and returns it to the secretary. Voting papers are then arranged alphabetically and scrutinised by reference to the list of proxies lodged, Register of Members, and the voting value of the shares held. The invalid voting papers are rejected and the number of votes for and against are reported to the chairman who declares the result of voting.

Voting.

The articles of a company prescribe the procedure to be observed in connection with voting at general meetings, and the prescribed regulations must be strictly followed. Usually the vote is taken by a show of hands. Everyone present who is entitled to vote has one vote only, irrespective of the fact that he also holds a proxy for an absent member. The compulsory regulation 56 of Table A provides that the chairman's declaration that a resolution has been

carried shall (unless a poll is demanded) be deemed conclusive evidence of the fact.

Decisions of members are obtained by putting the question to the vote, the chairman announcing the result. If a motion is carried *unanimously*, it means that every member present has voted for it; if it is carried *nem. con.*, it means that none has voted against it, though there may be some members who did not vote at all. In other cases, the chairman simply declares as 'carried' or 'rejected'.

Minutes

There is a statutory obligation under section 83 to keep minutes of all proceedings of general meetings of the members of companies and also of board meetings. The secretary is the proper person to prepare such minutes, for which purpose he must, of course, be present at the meetings and take the necessary notes. It is advisable that the minutes be written up as soon as practicable after the meetings have taken place, in order that the secretary's memory may be able to assist in the interpretation of his notes, and help him to make good any omissions therefrom.

It is very important that minutes should always constitute a clear and succinct record of the proceedings to which they relate. The pages of the book should be numbered, and on no account may any spilt pages be removed nor any erasures made. Alterations, when necessary, should be effected by crossing out the incorrect words and adding such others as may be needed, the whole thing being done in a manner which will disclose the exact nature of the alteration. Every alteration should be initialled by the chairman at the time he signs the minutes as correct, after which none may be made. Occasions may arise when the minutes have to be produced as evidence in a court of law, and it is, therefore, very important that the minutes should be carefully written.

Under section 83, the minutes of general meetings of the company are open to the inspection of members, but the minutes of directors' meetings are not. Therefore it is necessary that minutes of general meetings and board meetings should be kept in separate books. The minute books should be provided with proper indexes.

Minutes are the written record of the proceedings at meetings. The practice with regard to the particulars to be included in the minutes varies considerably. Some favour a bare outline of the proceedings; while others burden the minutes with too many unnecessary details. The ideal should be between the two. Reports of meetings are similar to minutes in respect of recording the proceedings thereat. But a report may be verbatim or summarised, while the minutes simply record only a summary of the business transacted and the actual wording of the resolutions passed. Reports may consist of speeches and arguments, but minutes mainly record decisions.

The minutes should be headed somewhat as follows:—

"MINUTES of the Tenth Annual Ordinary General Meeting of the

Members of the Swadeshi Co., Ltd., held at the Registered Office of the Company, 25 Civil Lines, Agra, on Friday, the 9th March 1945 at 3.30 p.m."

The names of those who may be present at a meeting should be given as shown in the specimen minutes appearing in the following pages.

Each minute should have a serial number and heading in order that it may be properly indexed. The items should be recorded in the order in which they were taken at the meeting. All resolutions carried should be set out in full, each forming a separate paragraph preceded by the word "RESOLVED", so that the actual resolutions stand out from any introductory or other matter. Where the chairman has mentioned the numbers voting for and against a resolution, the figures should be stated in the minutes.

Conduct of Business at General Meetings

Quorum. A quorum is the minimum number of qualified persons who must be present at a meeting before any business can be validly done. The articles fix the quorum. The quorum must be present until the close of the meeting. If no quorum is fixed by the articles, two members will form the quorum. Proxies are not counted in the quorum, but the representative of a company shareholder is counted.

Chairman. The chairman of the board of directors is appointed in the manner laid down in the articles. In India the chairman is usually one of the directors appointed by the managing agents. The articles also provide that the chairman of the board of directors shall be the chairman of the company. But if there is no such provision or the chairman is absent, the members present can choose some one of their number to be chairman. If the chairman is appointed contrary to articles, the appointment is void even though all the members acquiesce in the appointment.

When a number of persons assemble and put a man in the chair, they devolve on him by agreement the conduct of that body. If the articles contain express provisions as to the conduct of meetings, those rules must be observed; but in the absence of appropriate regulations, the chairman must act fairly and to the best of his judgment.

The duty of the chairman is to see (a) that his own appointment is in order; (b) that the meeting is valid; (c) that the business is taken up according to the agenda, unless subsequently altered by the consent of the meeting; (d) that reasonable opportunity is given to all members to express their views; (e) that, in case of dispute, he decides who shall speak first and that he protects the rights of the minority; (f) that all business is within the scope of the meeting; (g) that he maintains order and decides points of order; (h) that disorderly persons are removed or else the meeting is adjourned; and (i) that the decisions are obtained in the prescribed manner.

Casting Vote. It is customary for the articles to give the chairman a second or casting vote in addition to the ordinary vote possessed by him as member, if the votes of members are equal. In the absence of express provision,

however, the chairman has no casting vote, at a common law he does not possess this privilege. If the chairman does not exercise his casting vote; or if he does not possess it, and the voting is equal, the motion is deemed not carried.

Supremacy of the Majority. The rule that the votes of majority bind the whole of the members is a cardinal principle of company law, unless some provision to the contrary is to be found in the articles. This principle is, however, subject to two limitations, viz.—that an extraordinary or a special resolution is passed by a three-fourths majority of the members present; and that the members act in conformity with the articles and the law.

Although the supremacy of the majority is absolute and complete, their powers must be used *bona fide* for the benefit of the company as a whole and not for their own benefit. The majority cannot use their power to practise fraud or oppression on the minority, nor can they do any illegal or *ultra vires* acts.

Motions. A motion is a proposition or proposal put forward at a meeting for discussion and decision whilst a resolution is the formal declaration recording the actual decision by vote of the persons present at a meeting. Unless the motion is altered by an amendment, the words of the motion become the words of the resolution, and, in fact, a motion is really a 'proposed' resolution. Motions are sometimes described as 'the question before the meeting'.

The articles provide the procedure to be observed. Motions must comply with these regulations, be within the scope of the notice, and so framed that a definite decision can be arrived at. They should be in writing, signed by the proposer and handed to the chairman. Usually motions are seconded, but this is not necessary except where the articles require it.

Original motions are subject to amendment, provided the amendment is within the scope of the meeting. Amendments to an amendment should not be accepted; this leads to confusion and difficulty. The chairman may divide the motion into two parts, if by so doing he facilitates the business of the meeting. Where an amendment is carried, the original motion as amended becomes the substantive motion, and is capable of being further discussed and amended. A motion cannot be withdrawn without leave of the meeting.

Amendments. An amendment is a revision of the original motion under discussion either by the addition of certain words, the deletion of certain words, or a combination of both these methods. Although it is desirable that amendment should be in writing, signed and handed to the chairman, yet in the absence of any specific regulations, they may be moved verbally without notice.

An amendment must be relevant to the original motion, must be formally moved before the main question is put to vote; must not be a mere negative; and must be within the scope of the notice. It cannot be withdrawn without the leave of the meeting. If there are several amendments, the chairman will decide the order in which they are to be taken up.

The chairman must allow reasonable discussion on each amendment before it is put to the meeting. If the amendment is carried the original motion is revised accordingly and the revised motion becomes the substantive motion which may be further discussed and amended.

Speakers. Every member legitimately present has the right to speak once only on each motion or amendment. The mover of an original motion has the right of reply on the debate. The chairman will decide the order in which members shall address the meeting. A speaker should rise before the commencement of his speech, and address the remarks to the chair. He must confine his speech strictly to the question under discussion and resume his seat at its conclusion or (when a point of order is raised) on the chairman rising to address the meeting. The language used by a speaker should be courteous and should not be offensive or personal.

Interruption of Debate. When discussion on any particular question is going on at a meeting, it may be interrupted in one of the following ways :—

(a) **Amendments.** When an amendment is moved, discussion is diverted to the amendment until it is disposed of by the meeting. If it is lost discussion on the original motion is resumed; but, if carried, the motion as amended becomes the substantive motion and the latter may be further discussed.

(b) **Previous Question.** The object of this motion is to suspend the discussion of and the decision on an inconvenient motion which it is unwise to discuss in the general interests of the body or from the discussion of which no good is likely to result. It can only be proposed when the original question is before the meeting, and not during the discussion on an amendment.

The form in which it is put is "that the question be not now put." When the previous question has been seconded it is forthwith put to the meeting. No discussion is allowed. It takes precedence of all other business. If it is carried, the original motion is disposed of and cannot again be put before the meeting, i. e., is shelved once for all. If it is not carried, the original motion is put to the meeting without further discussion.

(c) **Net Business.** The object of this motion is to prevent a decision from being taken on the main question. Unlike the previous question it can be moved even when an amendment is before the meeting. It is put in the form "that the meeting pass on to the next business." After being moved and seconded, it is put to the meeting without discussion. If carried, the original motion is disposed of; if lost, the debate is resumed.

(d) **Closure.** If discussion on any question drags on and becomes unduly lengthy, and the mind of the meeting seems to be made up, this motion may be proposed with the object of avoiding waste of time and obtaining a definite decision on the question. The usual form of this motion is "that the question be now put." On being seconded it is voted upon without discussion. If carried, the main question is put to the meeting at once; if lost, the discussion is

resumed. The object of moving a closure is not to shelve the main question, but to secure an immediate decision.

(e) **Postponement.** A postponement, which should be distinguished from an adjournment, usually arises when the debate reveals some difference of opinion, and it is desired to obtain additional information on some points. It may be worded thus : "that further consideration of the motion be postponed until....." The mover of the original motion has the right of reply, after which it is voted upon. If carried, the debate is postponed to an agreed date ; if lost the debate is continued.

(f) **Adjournment.** The mover of the original motion has the right of reply to a motion for adjournment (either of the debate or of the meeting) except when the adjournment is for a short interval. The motion should state clearly for how long the meeting is to be adjourned, the date on which the adjourned meeting is to be held. The chairman on his own motion can adjourn the meeting with the consent of the meeting.

(g) **Disorder.** Discussion on motions is sometimes interrupted by the disorderly conduct of some members present. When there is persistent disorder, the meeting may be adjourned for a short time to enable order to be restored.

N. B.—For company meetings, where certain business must be transacted, e. g., the adoption or rejection of accounts, the previous question and the next business will be out of order, as their acceptance will prevent the meeting transacting the business for which it is convened.

Notices of General Meetings

The drafting of notices is an important duty of the company secretary. Since in many cases the managing agents of companies act as their secretaries, the notices are signed in several ways. Here are a few examples.—

(a) By Order of the Board,
X Co., Ltd. •

Managing Agents.

(d) By Order of Board.

X & Co.,

Managing Agents.

(b) By Order of the Board,
X Co., Ltd.,

Ram Lal,

Managing Director.

Managing Agents.

(e) By Order of the Board,
Ram Lal,

Managing Director.

(f) By Order of the Board,
Ram Lal,

Secretary or Manager.

(c) By Order of the Board,
X Co., Ltd.,

Managing Agents,

Ram Lal.

Managing Director

1. Notice of Statutory Meeting.

The Swadeshi Company Ltd.

NOTICE is hereby given that the Statutory Meeting of the above-named Company, pursuant to Section 77 of the Indian Companies Act of 1913, will be

held at the registered office of the Company, 25 Civil Lines, Agra, on Monday, the 12th March 1945 at 3-30 p. m., for the purpose of transacting the following business :—

1. Consideration of the Statutory Report.
2. Approval of modification in the contract between the Company and the Vendors, Messrs
3. Discussion of matters arising out of the Report or relating to the formation of the Company.

By Order of the Board,

Agra, 15th February 1945.

Or,

NOTICE is hereby given that, in compliance with Section 77 of the Indian Companies Act of 1913, the Statutory Meeting of the Company will be held at the registered office of the Company, 25 Civil Lines, on Monday, the 12th March 1945 at 3.30 p. m., for the purpose of considering the Statutory Report and transacting such business as under the provisions of the aforesaid section of the said Act should or may be transacted thereat.

By Order of the Board,

Agra, 15th February 1945.

2. *Notice of Annual General Meeting for doing only ordinary business.*

The Swadeshi Company Ltd.

NOTICE is hereby given that the fourth Annual General Meeting of the Company will be held at the registered office of the Company, 25 Civil Lines, Agra, on Monday, the 12th March 1945 at 3.30 p. m. for the purpose of transacting the following business—

1. To receive the Directors' Report and to pass the audited accounts for the year 1944.
2. To declare dividend.
3. To elect directors.
4. To appoint auditors and to fix their remuneration.
5. To transact any other ordinary business that may be brought before the meeting.

The share Books of the Company will be closed from 26th February 1945 to 12th March 1945 both days inclusive.

By Order of the Board,

Agra, 15th February 1945.

N. B.—The dividend, when sanctioned will be made payable at the Bank, Ltd., Agra, on and after the 20th March 1945 to those shareholders whose names stand on the Register of the Company on the 12th March 1945, to whom dividend warrants will be posted. Shareholders are requested to kindly notify any change of address giving ledger folio.

3. *Notice of Annual General Meeting for doing both ordinary and special business.*

The Swadoshi Company Ltd.

NOTICE is hereby given that the fourth Annual General Meeting of the Company will be held at the registered office of the Company, 25 Civil Lines, Agra, on Monday, the 12th March 1915 at 3.30 p.m., for the purpose of transacting the following business :—

As Ordinary Business :

1. To receive and consider the annual accounts for the year 1914 ;
2. To declare dividend ;
3. To elect directors ,
4. To appoint auditors and fix their remuneration.

As Special Business, to consider, and if thought fit, to pass with or without modification the following as a Special Resolution :—

That Article 134 (11) (ii) of the Articles of Association of the Company be altered by inserting in the first line the words 'second or subsequent' between the words 'first' and 'mortgage', and by adding a comma after the said word 'first,' and by inserting in the same line the words 'whether issued in rupee or sterling currency, between the words 'debentures and 'of and by substituting in the third last line the figure '5' for the figure '10 between the words 'during each of the' and the words 'years immediately preceding.'

The Shares Books of the Company will be closed from 26th February 1915 to 12th March 1915 both days inclusive.

By Order of the Board,

Agra, 8th February 1915

1. Notice of Extraordinary General Meeting held immediately after Ordinary Meeting.

The Swadoshi Company, Ltd.

NOTICE is hereby given that an Extraordinary General Meeting of the Company will be held at the registered office of the Company, 25 Civil Lines, Agra on Monday, the 12th March 1915 at 4.30 p.m., or so soon thereafter as the Fourth Ordinary General Meeting to be called on the same day shall be concluded, when the subjoined Resolution will be proposed as Special Resolution :—

The wording of the resolution as in No. 3 above.

By Order of the Board,

Agra, 8th February 1915.

N. B.—The words 'or so soon thereafter as the Fourth Ordinary General Meeting to be called on the same day shall be concluded' will not be necessary in a notice convening an extraordinary general meeting, if the extraordinary meeting is not held on the same day on which the ordinary general meeting is to be held.

5. *Notice of Half-yearly Ordinary General Meetings.*

When a company holds half-yearly ordinary general meetings, as is the case with many companies in this country, the first half-yearly meeting in the year takes the place of the annual general meeting, and it is at that meeting that directors are elected and auditors are appointed; while at the second half-yearly meeting held in the year these two items do not come up before the members. Thus the business for the first half-yearly meeting will consist of consideration of accounts, declaration of dividend, election of directors and appointment of auditors; and the business for the second half-yearly meeting to be held in the year will be only the consideration of accounts and the declaration of dividend.

Minutes of General Meetings

1. *Minutes of the Statutory Meeting.* (See Notice No. 1 above)

The Sawjoshi Company Ltd.

MINUTES of the Statutory Meeting of the Company held at the registered office of the Company on Monday, the 12th March 1945 at 3.30 p. m.

Present : Chairmen.

. }
 }
 } Directors.
 }

and 15 other members.

1. Notice of Meeting. The notice dated 16th February 1945 concerning the Meeting was read.
2. Statutory Report. The Chairman made an inaugural speech about the formation of the Company and its prospects, and then invited discussion and questions on the Statutory Report and matters relating to the formation of the Company. The questions put forward by the members having been answered, it was resolved, on the motion of the Chairman seconded by Mr., that the Statutory Report of the Company be adopted.
3. Modification of Contract. On the motion of the Chairman, seconded by Mr. it was resolved that the following modification in the contract dated between the Company and the Vendors, Messrs be approved :—
 "The purchase price of Rs. 5,00,000 be paid as to Rs. 1,00,000 in cash and the balance in fully-paid shares of the Company instead of Rs. 2,00,000 in cash and the balance in fully-paid shares as originally agreed."

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|------------------------------|--|
| 25. Notice of Meeting | The notice of the meeting dated 8th February 1945 was read. |
| 26. Adoption of Accounts | On the motion of the Chairman, seconded by Mr. it was resolved that the audited accounts of the Company for the year 1944 be adopted. |
| 27. Declaration of Dividend | On the motion of Mr. seconded by Mr. it was resolved that, as recommended by the directors, a dividend of Rs. 5 per share on 2,000 shares of the Company be declared for the year 1944, and that the dividend be paid to those shareholders whose names stood on the Company's Register of Members on the 12th March 1945. |
| 28. Election of Directors. | On the motion of Mr. seconded by Mr. it was resolved that Mr. X be re-elected and Mr. Y be elected as directors of the Company. |
| 29. Appointment of Auditors. | On the motion of Mr. seconded by Mr. it was resolved that Messrs. of be reappointed auditors of the Company for the current year on a remuneration of Rs |

30. Alteration of Articles, On the motion of the Chairman, seconded by Mr. the following resolution was passed as a Special Resolution :—
 " " as given before.

Meetings of Directors

The management of a company is carried on by its directors, who meet together for the transaction of the company's business at what are called Board meetings. The business that comes up before board meetings varies in the case of different companies. Matters which in the case of one company are dealt with by the directors, may in another be left to the managing agents or the managing director. The exact nature of business to be done at board meetings depends upon the articles of association. There are, however, certain matters, such as the allotment of shares, making of calls, forfeiture of shares, affixing the company's seal, issue of debentures, disposal of profits, etc., which can be dealt with only at board meetings.

Matters considered by directors at board meetings are usually decided by a bare majority ; but in some special cases the law requires a statutory majority of the directors. Thus the managing agents of a company cannot enter into any trading contracts with it without the consent of three-fourths of the directors present at a board meeting and entitled to vote on the resolution ; nor can the managing agents of a company invest the funds of one company in the shares and debentures of another company under their management unless the purchase has been previously approved by a unanimous decision of the board of directors of the purchasing company. In these two cases, therefore, a bare majority of the directors is not enough.

Directors' meetings are held periodically. The directors are usually empowered by the articles to transact business either by meetings or by correspondence. The procedure at board meetings is less formal and is governed by the articles and the directors' own resolutions.

The secretary, after consultation with the chairman of the company, should prepare an agenda for each board meeting. The provisions in the articles affecting board meetings and matters incidental thereto should at all times be borne in mind with a view to safeguarding the directors against unwittingly exceeding the powers conferred upon them. Preparation for, and proceedings at, meetings provide duties which occupy a very large portion of the secretary's time. The preparatory work for directors' meetings often includes summarised reports on the company's business, the collation of various documents and other information which will be required at the meetings, whilst the proceedings will provide the secretary with various instructions and duties.

The secretary's duties before, at, and after the board meetings may be as follows :—

1. To prepare agenda and issue notice of the meeting to directors.
2. To arrange for the attendance at the meeting of other officials of the

manner as the minutes of company meetings. If the directors have decided anything by correspondence, it is essential that such a decision should also be recorded in the Directors' Minute Book with a note that it was reached by correspondence and not at a meeting.

Agenda and Minutes of Directors' Meetings

1. First Meeting of Directors.

Agenda

1. Certificate of Incorporation
2. Appointment of Managing Agents.
3. Appointment of Bankers.
4. Appointment of Auditors.
5. Company's Common Seal.
6. Agreement with Vendors.
7. Underwriting of Shares.
8. Draft Prospectus.

Minutes

The Swadeshi Company Ltd.

MINUTES of the First Meeting of Directors held at the Registered Office of the company on Monday, the 12th March 1945 at 12 noon.

Present: Chairman

 Legal Advisor

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- | | | |
|---|--------------------------------|---|
| 1 | Certificate of Incorporation | Mr....., the Company's legal adviser, produced the certificate of incorporation of the Company No. 67845 dated.....for the inspection of directors. |
| 2 | Appointment of Managing Agents | Resolved that Messrs Prem & Co. be appointed the first managing agents of the Company with effect from.....upon the terms contained in the Articles and set forth in the draft agreement made between the Company of the one part and Mr. Ram Lal, Mr. Sham Lal and Mr. Mohan Lal carrying on business under the name of Prem & Co. of the other part; that the said agreement be hereby approved and that it be signed by Mr.....and Mr.....(directors of the Company) on behalf of the Company. |
| 3 | Appointment of Bankers | Resolved that the.....Bank, Ltd., is appointed Bankers to the Company; that the |

said Bank is hereby authorised to debit the Company's account with all cheques drawn upon such account, when signed for and on behalf of the Company by the managing agents; and that all cheques and other instruments requiring the endorsement of the Company may be endorsed for and on behalf of the Company by the managing agents.

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|---|-------------------------|---|
| 4 | Appointment of Auditors | Resolved that Messrs....., Registered Accountants, be appointed auditors of the Company on a remuneration of Rs..... |
| 5 | Common Seal | Resolved that the seal (of which an impression is affixed to these minutes) be adopted as the Common Seal of the Company, that a key of No. 1 lock of the Seal be held by the Chairman, and a key of No. 2 lock be held by the managing agents, and that the duplicate keys be deposited with the Company's Bank. |
| 6 | Agreement with Vendors | Resolved that the draft agreement dated..... made between the Company of the one part and Messrs..... of the other part for the sale of Messrs.....'s business to the Company as a going concern as from..... be approved and signed by Mr..... and Mr. (Directors of the Company). |
| 7 | Underwriting of Shares | Resolved that the terms on which Messrs..... have offered to underwrite 2,000 shares of the company be accepted, and that the Company's acceptance be communicated to them. |
| 8 | Draft Prospectus | Resolved that the draft Prospectus be approved; that the Prospectus be dated; that it be signed by all the directors, and that a signed copy be filed with the Registrar of Joint Stock Companies. |

2. *Subsequent Meeting of Directors.*

Agenda

1. Minutes of previous meeting
2. Resignation of Mr. W a director,
3. Appointment of Director to fill casual vacancy.
4. Report of Transfer Committee.
5. Purchase of additional machinery.
6. Investment of Reserve Fund.
7. Declaration of an interim dividend.
8. Appointment of a Committee of the Board.

Minutes

The Swadeshi Company Ltd.

MINUTES of a meeting of Directors held at the Registered Office of the Company on Friday the 22nd August 1947 at 12 noon.

Present : Chairman

 } Directors

 }
 Legal Adviser

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- | | |
|--------------------------------------|---|
| 81 Minutes of Previous Meeting | Minutes of the Board meeting held on..... were read and confirmed. |
| 82. Resignation of Mr. W | It was resolved that the resignation dated..... of Mr. W, a director, be accepted with regret and take effect from this date. The Board, however, takes this opportunity of recording its appreciation of his services to the Company. |
| 83. Filling of Casual Vacancy | Resolved that Mr. X be appointed a director of the Company in the place of Mr. W (who has resigned) for the remainder of the period for which Mr. W was elected, viz., until the annual general meeting to be held in 1946. |
| 84. Report of Transfer Committee | The Report of the Standing Transfer Committee of the Board was considered. It showed that applications were received for the transfer of 250 shares from fifteen shareholders, all of which except one from Mr. R were accepted and the transfers were given due effect to. It was resolved that the said Report be accepted. |
| 85. Purchase of Additional Machinery | It was resolved that the managing agents' proposal for the purchase of.....machinery at an approximate cost of Rs.....be approved and that they be authorised to place the necessary orders. |
| 86. Investment of Reserve Fund | Resolved that a sum of Rs. 1,00,000, representing the Reserve Fund of the Company be invested in the 3 per cent. Victory Bonds 1957, and that the interest to be received therefrom be credited to the Reserve Fund. |
| 87. Declaration of Interim Dividend | Resolved that an interim dividend at the rate of Rs. 3 per share free of income tax on 2,000 Shares of the Company be declared on account |

88. Appointment of a
Committee

of 1947 and that it be payable to those shareholders whose names stand in the Company's Register of Members as on 22nd August 1947. Resolved that a Committee of the Board, consisting of Messrs... .. (with Mr as the convener) be appointed to examine thoroughly the proposal of starting a retail branch of the Company in the East Punjab, and to report to the Board before the end of December next.

Dividends

Dividends are the profits distributed to shareholders, either on a percentage basis or at a fixed sum per share on the issued capital of the company. Where shares are not fully paid it is usual to pay dividends on the amounts paid up on such shares, and not on the nominal value, provided there is nothing contained in the articles to the contrary.

Where there is a special class of shares carrying preferential rights as to dividends, provisions defining such rights are sometimes contained in the memorandum but it is in the articles that the secretary will find the regulations relating to the disposal of the profits of a company. Usually, the directors are authorised (when the profits allow) to declare and pay interim dividends, but the sanction of the company in general meeting has to be obtained before the final dividend for the year is paid. In the latter case, regulation 93 of Table A, which is compulsory for all companies, provides that no dividend shall exceed the amount recommended by the directors.

Again, regulation 97 of Table A, which is also compulsory, lays down that no dividends shall be paid otherwise than out of profits of the year or any other undistributed profits. No dividend can therefore be paid out of capital, except in the special circumstances mentioned in section 107 which provides as follows:—

Where shares are issued for raising money to be spent on the construction of works and no profits can be earned for a long period, the company may pay interest on the capital so raised, though no profits are earned, if,

- (a) such payment is authorised by the company's articles,
- (b) the sanction of the provincial government has been obtained,
- (c) the payment is made only for such period as the provincial government may fix, but this period shall not extend beyond the half-year next after the half-year during which the works have been completed;
- (d) the rate does not exceed four per cent per annum,
- (e) the accounts of the company show the share capital on which and the rate at which interest has been so paid.

The object of these provisions is to make some compensation to shareholders for the delay caused to the company in reaching a revenue-earning stage.

It will be clear from what has been stated above that the secretary has very little to do with the actual declaration of dividends. His duties commence when declaration has actually taken place, and are as follows :—

Publication of Dividend. Where the shares of a company are to any extent held by the public, it is usual to send a notice to the press regarding the dividends declared. Below is given a specimen notice regarding an interim dividend :—

The Simplex Mills Company, Ltd.

NOTICE IS HEREBY GIVEN that at a Meeting of the Board of Directors of the above Company held this day, an AD-INTERIM DIVIDEND for the half-year ended 30th September 1944, at the rate of Rupees Four per Fully-paid Share of Rs. 50 each (free of income tax) was declared.

The dividend will be made payable at the Chartered Bank of India, Australia and China, Bombay, on and after Monday, the 15th January 1945, to those Shareholders holding Fully-paid Shares of Rs. 50 each whose names stand on the Register on the 15th December 1944, to whom Dividend Warrants will be posted.

Shareholders are requested to notify immediately any change of address to the undersigned.

The Transfer Books of the Company will be closed from Friday the 15th December 1944 to Friday the 29th December 1944 both days inclusive.

By Order of the Board,

Forbes, Forbes Campbell & Co., Ltd.,

Forbes Building,

Homo Street, Fort,

Bombay, 28th November 1944.

Agents.

As regards dividends to be declared at general meetings, their amount and rate are given in the Directors' Reports circulated to shareholders, but information as to how they are to be paid is included in the notices of the meetings. The following are a few examples taken from notices of ordinary general meetings appearing in the press :

1. As Dividend Warrants are sent only to registered shareholders or to their mandatories, shares on blank transfer should be submitted with completed transfer deeds for registration, before the Share Transfer Books are closed.

2. Dividend Warrants for the half-year ending 31st December 1943 will be posted to the shareholders at their registered addresses on and after the 30th March 1944. Intimation of any change in address should be given to the Company immediately.

3. The dividend and bonus when declared will be made payable at the registered office of the Company, on and after Thursday, the 22nd April 1943, between 12 noon and 3 p. m. on week days other than Saturdays, and between 12 noon and 1.30 p. m. on Saturdays to shareholders whose names stand on the Register of Members on the 1st April 1943.

The Swadeshi Company Ltd.

Agra,

10th March 1945.

Dividend Warrant No 237

To The..... Bank, Ltd.,

Agra.

Pay to Mr X on Order the sum of Rupees twentyfive only.

Rs 25 .

.....
Managing Agents.

Payee's Signature

N B.—This draft must be signed by the payee and presented for payment within two months.

2. Dividend warrant payable at the company's office.

The Swadeshi Company Ltd.

25, Civil Lines,

No 237

Agra, 10th March 1945.

DIVIDEND WARRANT for Rs 25 (Rupees twentyfive only), being dividend at the rate of Rs 5 per share, for the year 1944, without deduction of income-tax, on five ordinary shares in the Company standing in the name of Mr. X, payable at the Registered Office of the Company in Agra. This dividend was declared at the Tenth Ordinary General Meeting of the Company held on Friday, the 2nd March 1945.

We hereby certify that income tax on the entire profits and gains of the Company, of which this dividend forms a part, will be duly by us to the Government of India.

The Swadeshi Co. Ltd.

.....
Managing Agents.

(To be signed by the claimant)

Dividend Warrant No 237

I hereby certify that the dividend above mentioned relates to shares which were my own property at the time when the dividend was declared and were in possession of myself.

Signature of claimant.

Date.....

CAUTION. The above certificate must be carefully preserved as it will be required by the Income-Tax Officer when you claim refund of income-tax on this dividend.

.....Perforation.....

The Swadeshi Company Ltd.

Dividend Warrant No. 237

RECEIVED from the above-named Company Rs. 25/. (Rupees twentyfive only,) being dividend on shares specified in Dividend Warrant No. 237 for the year 1944.

Signature of Shareholder

Date.....

Witness.....

This formal receipt is being returned duly signed for payment. Please pay the amount at my cost by cheque, cash, money order, or postal order.

Signature of Shareholder

Date.....

Separate dividend warrants are usually prepared in respect of dividend due to a shareholder for the different classes of shares held by him. But in the interest of paper economy during the war only one dividend warrant is given for all dividends payable to a particular shareholder. Where a bank is acting as a mandatee for several shareholders, only one dividend warrant may be sent to the bank in respect of the dividend due to all such shareholders, but a separate Income-Tax certificate must be furnished to each shareholder.

Despatch of Dividend Warrants. Dividend warrants made payable directly by the company's bank are sent to the shareholders either on an application being made by the shareholders for them or without any such application. But dividend warrants payable at the company's office are always sent to shareholders without asking. If a company's articles so provide, it may always send dividend warrants by post without any application being made for them by shareholders.

Payment of Dividend Warrants. Where dividends are payable at the bank, a separate account should be opened at the bank for each dividend, the number of the dividend being used for purposes of identification, thus, 'Dividend No. 34 Account'. Before the dividend warrants are despatched, a cheque for the total amount payable should be drawn on the company's general account and paid into the dividend account, and at the same time a cancelled specimen of the dividend warrant should be sent to the bank. Information must also be furnished as to the signatures which will appear on the warrants. The Dividend Pass Book should be obtained from the bank periodically for checking purposes. The paid warrants should be marked off on the dividend lists, and a list made of all unclaimed dividends.

Where any dividend warrants are paid at the company's office, otherwise than by cheques, a note of the same should also be made on the dividend lists.

Filing of Return with I. T. O. Under section 19-A of the Indian Income-Tax Act 1922, the secretary must send to the Income-Tax Officer a return stating the names and addresses of company shareholders receiving dividend in excess of one rupee and also the names and addresses of those other shareholders

who receive dividends exceeding Rs. 5,000. Separate forms must be used for resident and non-resident shareholders.

Increase of Share Capital

The share capital of a company may be increased in two ways :—(a) By the directors issuing the unissued shares, and (b) By the company increasing its authorised capital and creating new shares for issue.

(a) **Increase by Directors.** Section 105 C provides that, where the directors decide to increase the capital of the company by the issue of further shares, such shares must be offered to the members in proportion to the existing shares held by each member (irrespective of class) and such offer shall be made by notice specifying the number of shares to which the member is entitled, and limiting a time within which the offer, if not accepted, will be deemed to be declined; and after the expiration of such time or on receipt of an intimation from the member to whom such notice is given that he declines to accept the shares offered, the directors may dispose of the same in such manner as they think most beneficial to the company. It means that if the directors of a company decide to issue the unissued shares, such shares must in the first instance be offered to the existing members *pro rata*. This is known as the shareholders' right of pre-emption.

The procedure to be adopted will be as follows :—

1. Consent of the Central Government must be obtained for the issue of the existing unissued shares under the Capital Issues (Continuance of Control) Act, 1947, if necessary

2. The directors will pass a resolution at the Board meeting offering the shares to the existing members, and authorise the issue of the necessary notice to be sent to the members, such notice specifying the number of shares to which the member is entitled and also specifying the date before which the offer may be accepted.

3. The Share Books of the company must be closed for some time by giving a public notice so that the notices to members may be prepared.

4. When a letter of acceptance together with the necessary money is received from a member the contract is complete, and no formal allotment is legally necessary, but in practice a formal allotment is made by the directors.

5. Any shares not taken up by the members will be disposed of by the directors at the best prices available for them.

6. A return of allotment must be filed with the Registrar.

7. Share certificates in respect of those shares must be prepared and sent to the members, and the necessary entries made in the Register of Members.

(b) **Increase by Shareholders.** Where the authorised share capital of a company is increased under section 50 by the creation of new shares, it is not legally necessary that such new shares should be offered *pro rata* to the existing members, unless the articles of the company in general meeting so provide. That is to say, in the absence of an express provision in the articles or in the absence

of a resolution of the company, the existing shareholders have no right of pre-emption in regard to new shares created by increasing the authorised capital.

The procedure to be adopted will be as follows:—

1. First of all, the directors will decide at the Board meeting that the authorised capital of the company should be increased.

2. Consent of the Central Government must be obtained for the increase of authorised capital under the Capital Issues (Continuance of Control) Act, 1947, if necessary.

3. Notices calling an extraordinary general meeting of the company will be sent to all members, accompanied by a circular explaining the need for the increase of capital.

4. At the general meeting of the company the necessary resolution will be passed authorising the increase of share capital. Section 50 requires only an ordinary resolution for the purpose; but the articles may specify either extraordinary or special resolution. The resolution must specify the amount by which the authorised capital is to be increased; whether the new shares are to be ordinary or preference or deferred; whether they are to be offered in the first instance to the existing members of the company, and if so, on what terms. The following is a specimen company resolution for increasing the authorised capital:—

That the Capital of the Company be increased to Rs. 30,00,000 by the creation of 60,000 new Ordinary Shares of Rs. 10 each ranking for dividend and in all other respects *pari passu* with the existing Ordinary Shares in the Company provided that such shares shall not participate in any dividend declared before 30th June 1945, in respect of profits accrued up to the 31st December 1944, but shall participate in any dividend declared thereafter *pro rata* with the existing capital.

That the said 60,000 new Ordinary Shares be offered in the first instance at a premium of Rs. 15 per share to the Ordinary Shareholders of the Company in proportion, as nearly as may be, to the number of Ordinary shares held by them respectively, and such offer be made by notice specifying the number of shares to which the member is entitled and limiting a time within which the offer if not accepted will be deemed to be declined, and that the Directors be empowered to dispose of the shares not taken response to such offer to such persons and upon such terms as they may deem expedient in the interests of the Company.

Note.—In this resolution Ordinary Shareholders alone (and not other classes of shareholders) are given the right of pre-emption in regard to the new ordinary shares. If the articles do not give any right of pre-emption to existing shareholders, nor is any given by the company's resolution, the resolution contains a clause like the following:—

"The Directors be authorised to issue the said shares to such persons to be paid up by such instalments or otherwise as the Directors may think fit, without being bound to offer the same or any of them to the existing members of the Company."

5. A notice of the increase of capital must be given to the Registrar within fifteen days from the date of the resolution, and the necessary capital duty paid.

6. The Share Books of the company must be closed for some time by public advertisement, so that the necessary notices be prepared for the members.

7. The directors will pass a resolution at the Board meeting offering the new shares to the existing members, and authorise the issue of the necessary notice to be sent to the members, such notice specifying the number of shares to which the member is entitled and also specifying the date before which the offer is to be accepted.

8. When a letter of acceptance together with the necessary money is received from a member, the contract is complete, and no formal allotment is legally necessary; but in practice a formal allotment is also made by the directors.

9. Any shares not taken up by the members will be disposed of by the directors at the best prices available for them.

10. A return of allotment must be filed with the Registrar.

11. Share certificates in respect of the new shares must be prepared and sent to the members, and the necessary entries made in the Register of Members.

Issue of Bonus Shares

Bonus shares are shares issued by a company to its members either fully or partly paid-up, out of accumulated profits in lieu of a dividend or bonus in cash. In other words, instead of profits being paid away in cash they are capitalised, retained in the business, and the members benefit by an allotment of shares instead of a payment in cash. The objects of issuing bonus shares may be—

(a) To bring the issued capital of the company in consonance with its present producing capacity, where the company is undercapitalised.

(b) To keep the future dividends of the company within reasonable limits, when its business and profits are steadily increasing.

Procedure. The following is the procedure to be adopted if a company wishes to capitalise its profits by the issue of bonus shares :—

1. Sanction of the Central Government under the capital issues (continuance of Control) Act, 1947, must be obtained for the issue of bonus shares.

2. There is no statutory authority for the capitalisation of profits by a limited company, and the shareholders are entitled to have their dividends paid in cash. Therefore the articles of the company must authorise the payment of dividend in specie, i. e. by the allotment of fully or partly paid shares of the company. If there is no such authority in the articles, a special resolution must be passed by the company in order to alter the articles with a view to taking the necessary power.

3. On the recommendation of directors, the company in general meeting

would pass an ordinary resolution declaring the bonus to be satisfied by the allotment of bonus shares. The resolution must be carefully worded so as to specify—

- (a) the amount of the Reserve to be capitalised ;
- (b) that the distribution is a capital bonus ;
- (c) what class of shareholders is to benefit, and at what date they must be registered ;
- (d) whether the shares are to be issued as fully or partly paid up ;
- (e) the date from which shares are to rank for dividend ;
- (f) the rate of distribution ;
- (g) the method of dealing with fractions ; and
- (h) that the directors are authorised to execute and file an agreement as required by law.

Below is given a specimen resolution dealing with all these points :—

"That it is desirable to capitalise a sum of Rs. 7,50,000, being part of the undivided profits of the Company, and that the said sum of Rs. 7,50,000 be capitalised and that this amount be used as a capital bonus which shall be applied on behalf of the persons who are on the 20th day of December 1944 holders of the 15,000 issued ordinary shares of the Company of Rs. 100 each in payment in full for 7,500 additional ordinary shares of Rs. 100 each and that such 7,500 additional ordinary shares credited as fully paid, which shall not confer the right to share in any dividend declared in respect of the half-year of the Company, ending on the 30th day of September 1944, but otherwise shall rank for dividend and in all other respects *pari passu* with the issued ordinary shares of the Company, shall be accordingly allotted to such persons respectively in the proportion of one of such 7,500 additional ordinary shares for two of the said 15,000 issued ordinary shares held on the said 20th day of December 1944 by such persons respectively, and that the additional ordinary shares so distributed shall be treated for all purposes as an increase of the nominal amount of the capital of the Company held by each shareholder and not as income."

"That pursuant to the above resolution and in satisfaction of the said special capital bonus the Directors be hereby directed to allot and distribute 7,500 additional ordinary shares credited as fully paid amongst the persons who are on the 20th day of December 1944 holders of the issued ordinary shares of the Company in proportion to the issued ordinary shares held by them respectively with full power to the Directors to make such provision by the issue of fractional certificates or otherwise as they think expedient in the case of fractions.

"That the draft of the Agreement providing for the allotment of the said additional shares in satisfaction of the said capital bonus submitted to this Meeting and signed in the margin by the Chairman thereof by way of identification be approved and that the Directors be authorised to affix the Seal of the Company to duplicate engrossments of such Agreement as and when the same shall

have been signed on behalf of the members holding ordinary shares in the Company on the 20th day of December 1944 by some person to be appointed by the Directors in that behalf.

4. The directors will nominate a shareholder to be a trustee for all shareholders, and then execute an agreement between the Company and the shareholders' trustee thereby constituting a right of the shareholders to the bonus shares.

5. The directors will make the allotment, provide for the adjustment of fractional parts of shares, authorise the issue of allotment letters and share certificates. In the case of fractions of shares, it is usual, to issue fractional certificates (or share coupons), which must be presented to the company on or before a certain date for being exchanged into a full share.

6. A return of allotment together with a copy of the contract showing the title of the allottees to the bonus shares must be filed with the Registrar, and the necessary entries made in the Company's books.

7. If the company has issued the whole of its authorised capital, its authorised capital must be increased in accordance with the provisions of section 50, before it can issue any bonus shares.

Reorganisation

Sometimes companies, even if they are earning profits, find themselves unable to pay dividends on share capital or even to meet their obligations to creditors without some alteration of their capital structure. This state of affairs is brought about in several ways. The company may be overcapitalised. In the course of its overcapitalisation it may have incurred heavy debts on which interest is due, whether profits suffice or not. The company may then, in order to stave off creditors by continuing to pay their interest, deplete its cash resources to such an extent that its trading is hampered and it has to borrow more money to continue its business. Many companies, hoping for a turn in their fortunes, have become deeply involved financially in this way until some interested parties, such as its debentureholders, call a halt and insist on remedial measures.

On the other hand a company may be able to pay the interest on its debentures and other loans and have profits remaining, but be unable to pay dividends because its share capital, through depreciation of its assets, is not intact, and should therefore be made good by the reservation, instead of the distribution, of profits.

In such circumstances as these a reorganisation is the usual course adopted. The essential principle of a scheme of reorganisation is that some, if not all, of the classes of shareholders and creditors make some sacrifice for the common good. If each class stood out for its exact rights, every class would suffer. It is not an easy matter to formulate a satisfactory scheme of reorganisation. There is generally much bargaining in which the powers of the various classes of creditors and shareholders to upset the company have to be taken into account.

When the debenture-holders' interests are in jeopardy, they usually have power to obtain the appointment of a receiver, who takes over the assets and runs the business on behalf of the debenture holders. He may have power actually to sell the assets, but without liquidating the company. The debenture-holders, however, may be persuaded that this course is detrimental to their interests; that the appointment of a receiver would so damage the prestige of the company that the assets would produce much less than the amount of the debenture-holders' claims, and that, therefore, a scheme of reorganisation, which would involve some sacrifice, possibly temporary, on the part of the debenture-holders, but which would at the same time enable the business to be continued, would eventually prove to their advantage.

Preference shareholders, who may not have received their dividend for a number of years and who, if their dividend is cumulative, may be entitled to past arrears, may be inclined to suggest liquidation, under which, according to the terms of issue, they may be entitled to be paid off at par with all arrears of dividend before the ordinary shareholders can get a single pie. But they will be told that a forced sale in a liquidation would, after providing for debentures and creditors, leave little or nothing for them. They are, therefore often persuaded to consent to a reorganisation involving probably not only a cancellation or funding of their arrears but also perhaps a reduction of their capital. In such a scheme, it is only fair that they should also be given a further share in future profits either by participating rights or by a free allotment of ordinary shares.

Frequently a reorganisation scheme is designed to provide new cash capital. If there are debentures already in existence this may mean the creation of prior debentures, the holders of the existing debentures agreeing to allow a new charge to be put before any charge they may have on the assets.

Reorganisation is the process of tearing down the old financial structure and using the materials in a new and stronger structure. In its proper sense, it is not merely a series of compromises and forced sacrifices imposed upon shareholders and debenture-holders. It is a rearrangement of the company's liabilities. If it is worked out on ideal lines, the reorganisation may be described as *a new financial plan which replaces the old plan that has proved faulty*.

Every scheme of reorganisation has one or more of the following objects:—
(a) To simplify the capital structure with a view to raising further capital; (b) To reduce fixed charges; (c) To eliminate past losses; (d) To pay or to fund pressing obligations; (e) To take care of accumulated preference dividends.

A reorganisation scheme should be adopted only when the company is out of the woods, that is to say, when it has started making profit and its operating losses have ceased.

Legal Procedure. Any scheme of reorganisation involving an arrangement between the company, its members and/or its creditors can be put through under the very comprehensive section 153. The scheme may involve a reorganisa-

tion of its capital structure or a compromise with its creditors. The outline procedure under this section is as follows :—

1. On the application of any company, member, creditor or liquidator, the court orders the holding of class meetings, as there may be various classes of shareholders and creditors affected. The procedure for the meetings is also laid down in the court's order, otherwise the procedure of the articles is to be adopted.

2. If, at the separate class meetings, the scheme is approved by a majority in number representing three-fourth in value of the members or creditors voting in person or by proxy, it becomes binding on all members and creditors after it has been duly sanctioned by the court and a copy of the court's order has been filed with the Registrar.

3. An appeal lies against the court's order.

If the reorganisation scheme involves a reduction of capital under section 55 or an alteration of capital under section 50, as it usually does in many cases, it will be necessary to observe the provisions of those sections before the scheme can be sanctioned by the court.

The reduction of capital becomes necessary under section 55, (i) when lost capital is to be written off in order to adjust the asset figures to values commensurate with their earning power with a view to the resumption of dividends and if necessary, the raising of fresh capital, and (ii) when superfluous capital is refunded to shareholders. If a company's articles permit the reduction of capital, it must first pass a special resolution and then apply to the court by petition for the confirmation of the resolution. When the court makes the order and confirms the petition, the order must be advertised, and the court may order the words 'and reduced' to be added to the name of the company for a short period, if there are any special reasons for doing so.

Under section 50, a company may alter its share capital by increase, by consolidation of its shares and division thereof into shares of larger amount, by conversion of its shares into stock or vice versa, by cancellation of unissued shares or by subdivision of its shares. Any of these things can be done simply by passing an ordinary resolution of the company, provided the articles contain the necessary authority. The articles may, however, prescribe an extraordinary or special resolution in place of the ordinary. When the capital is altered, necessary information must be sent to the Registrar, and in the case of increase of capital, additional duty, if any, paid.

N. B.—A Company's memorandum or articles of association may authorise the variation of rights attached to any class of shares in the company, subject to the consent of any specified proportion of the holders of the issued shares of that class or subject to the sanction of a resolution passed at a separate meeting of the holders of those shares. Such a variation of rights is not necessarily part of scheme of reorganisation. It may be, for instance, to get rid of an inconvenient provision that prevents a company from raising fresh

capital. Whatever the cause may be, even if the necessary consent has been given in accordance with the company's memorandum or articles, the shareholders who dissent from the variation have special rights of appeal under section 66-A. *Holders of not less than 10 per cent of the issued shares of the class affected may apply to the court within fourteen days to have the variation cancelled. The court may, after hearing the case, either disallow or confirm the variation.*

Reconstruction

The term 'Reconstruction' in relation to companies strictly refers to the sale of the business of an existing company to another company which may be already in existence or which may be formed for the purpose. The vendor company either goes into voluntary liquidation or is dissolved by the court. Such a reconstruction is resorted to (i) in the case of an unsuccessful company, for writing off lost capital and for raising additional capital by exchanging fully paid shares for partly paid shares, and (ii) in any other case, for obtaining new powers, for altering the registered office of the company or for purposes of amalgamation. Reconstruction may be brought about in the following ways :—

1. *Under the Memorandum.* When the memorandum confers the necessary powers, the directors may sell the company's business and undertaking (with the consent of the company in general meeting in the case of a public company or of a subsidiary company of a public company, as required by section 86-II), but the company must continue its separate existence either as a holding company with the shares in the transferee company as its principal asset, or if the business is sold for cash, by investing the proceeds in the purchase of new assets. If it is intended to distribute the sale proceeds amongst the shareholders and wind up the company, the reconstruction must be done under section 208-O.

Any scheme by which a company sells its undertaking under a power to do so contained in its memorandum, and provides for the distribution among its members of the shares or other consideration to be received from the purchasing company, is void unless it makes provision for the rights of dissentient shareholders.

2. *Under section 208-C.* A sale under this section becomes necessary when a company needs more capital and cannot get it without putting some pressure on the existing shareholders. To do this a new company is formed, and the old company, through its liquidator, sells its undertaking to the new company in such a way that each shareholder in the old company is entitled to one or more shares in the new. But whereas the shares in the old company were fully paid, those in the new company are only partly paid, so that each shareholder must either undertake a fresh liability for calls or give up his shares. This section, however, provides an ample safeguard for the rights of shareholders who dissent from the scheme provided they notify their dissent in the proper way.

*Note:—*Under this section, the sale of the undertaking of a company in

liquidation may also be made to another existing company and the consideration may be satisfied by fully paid shares. This will be the case where a company is being reconstructed for the purpose of amalgamation.

The legal procedure under the section is as follows :—

If a company is being or is proposed to be wound up altogether voluntarily, and its property is proposed to be transferred or sold to another company (newly formed or an existing one), the liquidator of the first company may, *with the sanction of a special resolution*, receive in compensation shares, etc., in the other company to distribute among the members of the first company. This will be binding on all the members of the first company. But, if any member who has not voted for the special resolution expresses his dissent in writing, addressed to the liquidator and left at the registered office of the company within seven days after the passing of the resolution, he may require the liquidator either to abstain from carrying the resolution into effect or to purchase his interest at a price to be determined by agreement or in default by arbitration.

Under section 209-F, the procedure outlined above also applies to a creditors' voluntary winding up with the only difference that instead of a special resolution of the company the scheme must be sanctioned by the court or by the committee of inspection.

3. *Under section 153 and 153-A.* A reconstruction or amalgamation can also be carried out as a scheme of arrangement under section 153, but in such a case, the court may require the rights of dissentient shareholders to be properly protected in the same way as under section 209-C. When a reconstruction or amalgamation is carried out under section 153, the court may, under section 153-A, make an order vesting the property of the vendor company in the purchasing company, and providing for the appropriation to the members of the vendor company of shares, etc., in the purchasing company, and providing for the dissolution of the vendor company without winding up.

Note.—The term reconstruction is also very often used for what are really reorganisation schemes as already explained above.

Amalgamation

An amalgamation and acquisition of controlling interests of two or more companies is carried out with the object of eliminating destructive competition and effecting economies in production, and of enlarging the scope of their activities. The amalgamation may be carried out as follows :—

1. Under section 151, 153-A and 208-C as already explained above, the business of one company may be transferred to another company, and the vendor company by being wound up or by being dissolved by the court disappears.

2. One company may purchase in the open market a sufficient number of shares of another company in order to give it a controlling interest in that company. Such a method is obviously not very practicable, as the price of the shares may rise to prohibitive heights.

3. Section 153-B makes provision for the amalgamation of companies under

a scheme which does not even require the passing of any resolution at meeting, and which may nevertheless be binding on dissenting shareholders. Thus, if the A Company, after consultation with the directors of the B Company, makes an offer to any class of shareholders of the B Company to buy their shares either for cash or for shares, and within four months the holders of the nine-tenths of the shares accept the offer, then the A Company may at any time within two months after the expiration of the prescribed four months give notice to any dissenting shareholders of the B Company that it desires to acquire their shares on the same terms as the original offer.

Unless on an application by the dissenting shareholders the court thinks fit to order otherwise, the A Company is entitled to acquire the shares. The matter is settled through the B Company. That is to say, the A Company hands over the consideration to the B Company, which thereupon has to register the A Company as the holder of the shares. The B Company has to account to the dissenting shareholders for the consideration it has received.

Test Questions

1. What qualifications should the secretary of a joint stock company possess in order to perform his duties efficiently? (*Agra M. Com. 1948*).
2. What are generally the duties of the secretary of a joint stock public company? (*Agra B. Com. 1942*).
3. Describe in detail the law and practice regarding the forfeiture of shares and the reissue of forfeited shares. (*Agra M. Com. 1948*).
4. Define a 'Share Certificate.' When must such certificates be issued to allottees and transferees, and what is the remedy of a shareholder whose certificate has been lost or destroyed? (*Agra B. Com. 1948*).
5. What precautions should a company secretary take before issuing a duplicate share certificate in place of the one lost by a shareholder?
(*Agra M. Com. 1947*).
6. In what ways can a joint stock company borrow money? What security can it offer?
(*Bombay B. Com. 1940*).
7. Describe briefly the secretarial practice relating to the transfer of a company's shares, and draft the notices that have to be issued to transferors and/or transferees.
(*Agra M. Com. 1945*).
8. Distinguish between transfer and transmission of shares. What procedure is followed in each case?
(*Agra M. Com. 1947*).
9. What statutory books and records are required to be kept by a company under the Indian Companies Act?
(*Agra M. Com. 1947*).
10. Summarise briefly the provisions of the Indian Companies Act relating to a company's Register of Members.
(*Agra M. Com. 1946*).
11. What is an annual return? What are its contents?
(*Agra M. Com. 1948*).
12. What are the rights of the shareholders of a public limited company regarding the inspection of and the obtaining of copies of (a) the account books

of the company, (b) the minute book of general meetings, and (c) the minute book of directors' meetings? Does the right to inspect also entitle shareholders to take copies themselves or through their agents? (*Agra B. Com. 1918*).

13. What do you understand by a special resolution? How is such a resolution passed by a company? Draw up one supplying imaginary details.

(*Agra M. Com 1947*).

14. Within what time is a statutory meeting required to be held? Is there any difference in regard to this meeting for a private or a public company? Draw up an agenda for a statutory meeting.

(*Agra B. Com, 1946*).

15. What business is usually transacted at the statutory meeting of a public company? Draft specimen minutes of such a meeting.

(*Agra B. Com. 1916*).

16. What is the legal provision for the holding of the ordinary general meeting of a company? What business is transacted at such meetings? What are the duties of the secretary in this connection?

(*Agra M. Com. 1918*).

17. Draft a short Directors' Report of a limited company as required by section 131-A of the Indian Companies Act of 1913.

(*Agra B. Com. 1945*).

18. Mention the nature of business that can be validly transacted at the statutory, ordinary and extraordinary general meetings of a limited company, and draft a notice (for insertion in a newspaper) calling a general meeting of a company which has a number of foreign shareholders, some of whom have no registered address in British India and have not supplied to the company an address within British India for the giving of notices to them.

(*Agra B. Com. 1944*).

19. Draft notices for the following company meetings, giving the number of clear days' notice required in each case :—(a) Statutory Meeting, (b) Meeting to alter the articles of association, and (c) Meeting to reduce the share capital.

(*Agra B. Com. 1948*).

20. What is the procedure to be followed at an annual general meeting of a joint stock company? Describe the duties of the secretary in connection with the meeting.

(*Bombay B. Com. 1942*).

21. Draft imaginary minutes of the annual general meeting of a limited company.

(*Alld. B. Com. 1940*).

22. Distinguish between statutory meeting, annual general meeting and extraordinary meeting of the shareholders of a company.

(*Alld. B. Com. 1937*).

23. Write (a) a notice calling an extraordinary general meeting of a company for the purpose of altering its articles of association, if the meeting is to be held immediately after the ordinary general meeting convened on the same date, and (b) a circular to shareholders explaining the reason for such alteration.

(*Agra M. Com 1945*).

24. Outline the general rules of procedure at company meetings in relation to resolutions, amendments and voting.

(*Agra M. Com. 1945*).

25. Draft in proper form the minutes of an annual general meeting of a limited company, at which, in addition to the ordinary business, some special business has also been transacted. (*Agra B. Com. 1945*).

26. What is meant by the closure and the previous question?

(*Agra B. Com. 1943*).

27. Draft an agenda of a meeting of the Board of Directors of a public company of about five items, and then proceed to write minutes on the same in proper form. (*Agra B. Com. 1947*).

28. What are the duties of a company secretary in connection with the meetings of its directors? (*Agra M. Com. 1946*).

29. Draw up the agenda and write out the minutes of the meeting of directors of a sugar mill company convened to consider and pass the annual accounts of the company. (*Agra M. Com. 1947*).

30. Draw up imaginary minutes in regard to the following four items considered and decided by the Board of Directors of a public limited company:—

(a) Election of six members and a convener of a sub-committee appointed to reorganise the capital of the company;

(b) Proposed alteration in the articles of association relating to the appointment of managing agents in place of the managing director;

(c) Appointment of auditors to fill a casual vacancy;

(d) Authorising the Chairman to raise a loan of Rs. 10,00,000 against the security of uncalled capital and the block account of the company at $4\frac{1}{2}\%$ per annum interest and repayable in instalments of Rs. 2,00,000 each year with interest. (*Agra B. Com. 1946*).

31. Describe briefly the secretarial practice relating to the payment of dividends by a company, and draft the form of a dividend warrant with income tax certificate attached thereto. (*Agra M. Com. 1945*).

32. What is the procedure to be adopted if a company wishes either (a) to increase its authorised capital or (b) to capitalise its profits? Draft a complete resolution for the purpose. (*Agra M. Com. 1945*).

33. What is a scheme of arrangement under section 153 of the Indian Companies Act of 1913? Explain the scope of this section and outline the procedure. (*Agra M. Com. 1945*).

34. Describe briefly the nature of a reconstruction scheme under section 208.C of the Indian Companies Act. (*Agra M. Com. 1945*).

35. Companies are said to be legal entities having a perpetual succession and a common seal. They also change form by means of 'reorganization', 'reconstruction' or 'amalgamation'. Briefly illustrate what you understand by these terms. (*Agra B. Com. 1947*).

36. How and under what circumstances can a company reduce its share capital? (*Agra M. Com. 1947*).

CHAPTER 6

INTERNAL ORGANISATION OF BUSINESS HOUSES

1. Retail Trade

The word retail is a French word with the prefix *re* and the verb *tailler*, meaning to cut. Evidently retail trade is one that cuts off smaller portions from larger lumps of goods. Retailing is to be regarded not merely as the means by which the consumers are supplied with small quantities of goods, but also as the last link in a gigantic chain of marketing. A retailer is an intermediary between the wholesaler and the ultimate consumer. He purchases from the wholesaler and sells in small quantities to consumers. He needs smaller capital than a wholesaler. Retail trade is carried on mainly on a cash basis, though credit may be allowed to regular and approved customers. A retailer has usually to carry a large variety of goods in his stock, and there is little specialisation in his trade. As a retailer has to appeal to a wider circle of the public an attractive shop front, good showrooms, expert salesmanship, suitable advertising and a central position in the market are essential for his success. A creation of local reputation will pay him considerably. The principal functions of the retailer are as under :—

(a) He helps the consumer in particular and the community in general. He prevents waste by supply of goods at the right time and in convenient quantities. He tries to satisfy his customers in every possible way, and his window-dressing, showrooms and scientific advertising are educative to the public. He keeps a large variety of goods manufactured by different concerns, with a view to giving his customers a good scope for choice and selection.

(b) He studies the taste, likes and dislikes of the consumers, and through the wholesaler he communicates to the manufacturer the results of his study.

A retail shop may be in the nature of a general store, or it may specialise more or less in one type of commodity. The village shops and the small shops that are found in the side streets in working class quarters of large towns are typical examples of the first type. Grocery, hardware, clothing and jewellery shops and bookstalls fall under the second category. Specialisation depends upon the extent of the market and the degree of competition. The work of the retail shop lies in the purchase and sale of goods so as to yield a profit to the proprietor. In order to achieve this object, a place must be provided where the goods can be displayed for the inspection of the public and sold; provision must be made for the storage of reserve supplies of goods, and finally the records of the business must be properly kept so that the proprietor may be able to ascertain the result of his trading. Hence a retail business requires a shop, a

warehouse and an office. The smaller the concern, the more will the last two tend to disappear, so that in a majority of cases only a shop is all that is enough.

A person, wishing to start a retail business, must carefully consider a number of factors before he decides to do so. First of all, he should decide upon the location of the shop. As a general rule, the busiest spot in the heart of a town or city is most suitable. Not infrequently it is seen in large towns that a particular locality often tends to acquire a reputation for a certain class of trade. After selection of a suitable site the external appearance of the shop must receive proper attention. The signboard must be placed over the front of the shop and must be in harmony with the external decorations, if any. Illumination at night will be an additional advantage.

Window-dressing is another important factor which should not be neglected. In the modern competitive age it is indispensable. It calls for artistic taste and a proper appreciation of beauty. The articles displayed in the window should bear a price card, for price is a determining factor, specially in India, with quite 90% of onlookers. Equal care must be bestowed on the interior decorations as well. The window-dressing may be of little avail unless the interior of the shop is equally good. This will require sufficient accommodation. In the interior of the shop arrangement should be made for the convenience and comforts of customers.

The strength of the office will depend upon the size and nature of the business. A shop which allows credit to its customers will of necessity entail more clerical work than one which transacts only cash business. It is absolutely essential that a proper record should be made of every transaction—cash or credit—so that complete control may be exercised over the sales. In the majority of cases this control is exercised by the use of duplicate counter books. At the end of the day the cash in hand must be equal to the total of the duplicate cash memos and the opening balance, if any. The shop assistant must consult the office while granting credit to the customers except, of course, in the case of well-known customers. The posting of credit memos is made to the debit of customers' accounts. (With regard to purchases of goods, every invoice received must be fully checked before it is entered in the purchases book, and all payments must be promptly made.)

The management of the warehouse needs special attention. Goods must be arranged in such a way as to ensure economy of space and time and prevent pilferage. A proper stock book must be maintained. As soon as a shop is secured and the necessary initial stock purchased, the proprietor must find out ways and means of increasing his sales. The trader, in his own interest as well as in that of his customers, should scrupulously avoid the principle of 'buying in the cheapest and selling in the dearest market'. 'Small profits and quick turn-over' should be his motto, by which he will get his turnover at proportionately lower cost in expenses, keep his stock always new and fresh, and he will need a smaller amount of capital. Comparatively cheaper price is a magnetic force, and customers naturally cluster around it to satisfy their demands.

In order to attract customers a retail trader may have to use some or all of the following devices :—

1. Window display and counter display are most effective forms of advertising. A cleverly dressed window draws the attention of potential buyers more easily than newspaper advertising and is more satisfying to the would-be purchaser. The pillars and columns of the building may be frequently provided with show cases, and the external appearance of the shop should receive due attention. A progressive retailer spends considerable sums on them. The internal equipment of the shop should be in line with the window display. The goods should be so arranged that every article may be visible, result in economy of space, and present a pleasing appearance to the eye.

2. The demand of customers should be aroused by means of suitable advertising, so that they may be persuaded to pay a visit to the shop. A trained salesman may be the backbone of the success of a retail house. The customers should be treated neither with disdain nor with excessive servility. The shop assistants should be instructed to be always polite, courteous and attentive to the customers.

3. Clearance sales are usually organised at the end of a season. They are intended to draw customers in large numbers. It pays a shopkeeper to sell two articles at the reduced price than to sell one at the regular price. Obsolete and shop-soiled goods must be cleared at reduced prices.

Pricing. The greater the sales, other things being equal, the larger the profit. There is always an inverse correlation between the price and the turnover. Low price is an inducement for a would-be purchaser to purchase. Prices in the retail trade therefore materially affect sales. The following factors usually determine the fixing of prices in retail trade.

1. The prime factor is the cost of the goods itself, and unless the cost is recovered the concern is bound to come to grief. If, however, the margin of profit is lowered because the prices have been forced to be reduced, the remedy would lie in the curtailment of expenses.

2. The prices charged by competitors exercise the greatest influence in fixing the price of an article. As a rule the prices fixed for the various goods must be in line with those of competitors.

3. The articles sold by retailers may vary in quality and also in price. A shop which is situated in the heart of the town and is reputed for high class goods usually charges a higher price than an average shop. To a certain type of mind there is a close association between quality and price and such people always choose a dearer article in order to obtain, as they imagine, the best quality without any further examination.

4. The prices which customers have been accustomed to pay should always be taken into consideration in fixing the price of an article. Of course it is a good policy to change the quality of an article if the circumstances so demand rather than to change the customary price.

5. Working expenses are closely related to the question of price-fixing. Unless these are correctly ascertained, there is no sound basis for fixing the selling price. The test of a good and efficient management is the maintenance of the working expenses at a comparatively lower level.

Large Scale Retailing

This is the age of mass production and mass distribution. There is a growing tendency for business to develop into large units, the urge behind it being chiefly the desire to eliminate competition as far as possible. During the present century productive and distributive concerns have increased very greatly in number and in general efficiency, thereby leading to keener competition than ever before. Firms on the margin of efficiency disappear under the stress; those remaining in the struggle find their profits reduced owing to the cutting of prices in the fight for orders. The buying up of the less successful by the more successful firm and the amalgamations that are frequently taking place are evidence of the desire to curb such competition and, either by maintaining price levels or by internal economies, to keep up the return on the capital invested. This is going on not only in production but also in distribution.

Large scale retail houses find it economical to centralise their buying operation. The large quantities ordered make possible considerable savings on purchases from wholesalers or direct from manufacturers which may be passed on to the consumers or retained as extra profit. The large capitalisation enables the firm to carry a great assortment of goods which also attracts customers. It is, however, remarkable that while there has been a steady growth in combinations of business units, the small trader has not been eliminated, but in some fields has almost completely held his own. He retains his business usually by specialising in some particular line on which he makes a reputation, recognising his inability to cope with the great variety of goods the large firm stocks. Moreover the personality of the small trader is felt throughout his business, while the large scale units lack this distinctive feature. It is for these reasons that in the face of large scale retail concerns the small shop-keeper still exists. In fact, he cannot be driven out of existence so long as the personality of the proprietor of a business counts. The two forms of large scale retailing are departmental stores and multiple shops.

1. Departmental Stores

A departmental store is really the opening, under one roof and under one control, of a number of shops each dealing in a certain line of goods. The idea of a departmental store is to provide a large variety of merchandise from a pin to a motor car. Departmental stores originated to cater for the richer customers who care for quality and service which cannot be supplied by smaller retailers. The growth of such stores is largely due to the pursuit of this policy: and departmental stores of world-wide fame such as Harrods, Selfridges, Gammages, Army and Navy Stores, etc., have prospered remarkably

as a result of attention to service and extreme regard for the customers' wishes.

A departmental stores, as the name implies, consists of a number of departments, each dealing in one particular line of goods. There may be drapery department, toilet department, leather goods department, books department, watches and clocks department, bicycle department, and so on. It is said that a person can usually purchase everything he needs in a departmental stores.

Location. The success of a departmental stores depends upon the number of customers it can attract, and therefore its situation should be such as is most frequented by rich people. It must occupy a central position. Its premises are usually very extensive, giving special convenience to all shoppers, whether buying or not. Under the guise of 'service' the modern departmental stores has come to be a sort of club or amusement place for people. One ordinarily finds in the stores rest room, reading and writing rooms, restaurants, information bureaux, post office, telephone booths and telegraph stations for the unrestricted use of all. In some stores lectures, demonstrations, music programmes, moving picture shows, even operas and plays are given frequently. Each department in the larger stores is of a size comparable to a shop in itself, but the departments are connected and allow of perambulations throughout the interior of the buildings. This combined with the method adopted of displaying all goods for inspection brings before the possible customer the whole contents of the stores, offering a wide choice and every inducement to buy.

Organisation As most of the departmental stores are owned by limited companies, the board of directors determine the general policy of the stores, but they delegate to others the power to carry it out. The executive head of a departmental stores is the managing director who acts on behalf of the board of directors. In close touch with him there may be the general manager who coordinates the work of the various sections in consultation with the section managers. Each section manager is in turn responsible for the success of the departments forming the section, but leaves considerable freedom of action to the departmental managers. The secretarial and accounting sections may be directly responsible to the managing director. The desk cashiers in each department are included in the accounts section, which also records all the departmental statistics. The production section will need a system of costing. In fact, each department will have its costing records to see what its quota is towards the general profits. Accounting and other functions are carried on for all departments by the central accounting section, but each department will have to bear its proportion of the cost in order to arrive at a true profit.

Each department in a departmental stores is in charge of a manager who in most cases is the chief buyer for the department. He is responsible to the section manager for its success. The stock figure for each department is not a

static one, but is governed by the amount of business done. A prescribed rate of turnover of stock is expected from each department according to the class of goods in which it deals. Provided that the prescribed rate is reached, the department is practically free from any restriction upon the amount of stock it should carry. Departmental stores must advertise. They attract customers from places far removed from the area in which they are situated. In many cases each department or group of departments is brought to the notice of the public in turn by press advertisements or by special offers for limited periods.

Advantages. The departmental store enjoys the benefits which accrue to all large scale enterprises, the most outstanding of which is its ability to purchase goods cheaply. Moreover it can afford to utilise the services of experts to conduct the buying for each department. In addition to these economies in buying, it can also secure economies of administration. As a departmental store is usually located in a central position, it can secure large customers. In fact, the provision of facilities under one roof, which enable a customer to satisfy all his requirements, is in itself a great attraction. The resources of the departmental stores enable it to spend large sums on advertising. Again when customers enter the store to deal with one department, they are very frequently induced by the advertisement which the display of goods offers to make purchases in other departments as well. The services performed by the departmental stores, including those which are outside the ordinary scope of business, constitute an attraction to a certain class of the people.

Disadvantages. On account of the expensive services rendered and heavy overhead expenses, the cost of doing business often becomes very high. The fact that a departmental store is usually located in a central shopping area is not always an advantage, because goods that are wanted at short notice are usually purchased from smaller traders found near the homes of consumers. The customers of a large departmental store do not as a rule receive the same personal attention as they do from smaller retailers. To many people the personal element has a very powerful appeal, and with regard to such people the departmental store is at a disadvantage.

Departmental stores are very common in Europe and America; but this form of retail trade organisation has not made much progress in India. The departmental store requires large rich clientele which is generally not found in this country. The towns which offer this condition are not many. Departmental stores can flourish only in towns like Bombay and Calcutta where there are some already in existence. The population of the country consists largely of middle class people who care more for cheapness than for quality. It is the price that principally matters to them. Departmental stores usually charge higher prices than is the case with ordinary retailers.

2. Multiple Shops

People in India are not generally familiar with the staggering growth in Europe and America of trading organisations known as multiple shops or chain

stores. Multiple shops are called chain stores in America. The multiple shop system is the opening of shops in different towns by a business unit which may be a company, a partnership or a sole trader. The best examples of multiple shops in India are afforded by Bata shoes and Singer Sewing Machine shops. A Bata shoe shop is found in almost every town throughout India. The first principle of multiple shops is specialisation. They specialise in a limited range of merchandise which should have a direct and popular appeal to the customers. The whole secret of success in this line of trading depends upon the selection of the goods that are to be offered for sale.

The shops are opened in different towns in contrast to a departmental store which is usually in a central shopping area of a particular town. The multiple shop system takes the goods to the residential area and saves the purchaser the need to travel.

Organisation. The multiple shops are under central control. A manager is appointed for each shop and he is responsible to the Head Office for its success. The stock is supplied by the central depot. Many of the multiple shop firms are producers of the goods they sell, e.g. Bata. In other firms nothing is produced and the stock is purchased by the central office for the shops. Some manufacturing concerns which retail their products under the multiple shop system also buy goods for stock from other manufacturers. The shop managers are restricted in their activities. They are salesmen of the goods received from the central depot.

The takings of each shop have to be remitted to Head office usually by payment to a local bank, and the expenses of the shop are paid by a separate cheque. Some firms may, however, allow such expenses to be deducted from the takings and only the balance remitted. The manager of each shop makes out returns of cash takings and for stock required. The Head Office keeps the accounts for the various shops and incorporates them into the general accounts of the business. For accounting purpose the goods sent in the shops are recorded at selling price which makes the stock calculations easier. The shop manager must agree his takings plus stock on hand plus credit sales (if any) with the amount of goods invoiced to him. Inspectors are appointed to make unexpected visits to shops to ensure that appearances and tone are maintained at the required standard, and stock-takers also make unexpected calls to check and to prevent fraud.

It is important in the administration of all multiple shop concerns to adopt standardised and uniform methods for all shops. Without standardisation the supervision and control of a large number of shops would be practically impossible. If separate methods were adopted for every shop the management would have to review its policy and consider its decisions in the light of the conditions at each individual shop. When the policy throughout is uniform, decisions can usually be made effective to all shops with confidence in the knowledge that what is

considered advisable for one shop should be suitable for all others similarly placed.

The multiple shop system has adversely affected the position of small retailers, though it has not completely ousted them. The multiple shop creates a demand for a standard article which is obtainable in like quality wherever a purchaser goes, but the central buying, though it may save on large purchases, involves a central depot and that necessitates double transport, that is, from producers to depot and from depot to shops. The single shop avoids this extra cost by getting its goods direct from the producer or wholesaler. The saving is mainly with such firms as retail their own products in avoiding the middleman's profit, but that advantage is felt only if the manufacturing side of the business is large enough to produce as cheaply as the manufacturers who do not sell retail. Where the small retailer may feel the competition of the multiple shops is that he must make a sufficient profit, whereas the multiple shop can hold on to a branch so long as it pays its way.

Advantages. As the goods are purchased or manufactured on a large scale and as intermediary profits are eliminated, the prices charged to customers are reduced to a minimum. Experts in all phases of Head Office work may be employed and their services fully utilised. The uniformity of branches makes them easily recognised by the purchasing public, and the goodwill attaching to one branch thus tends to flow to other branches. Advertising may be employed with advantages to all branches. Branches may obtain any necessary supplies from the central depot at short notice; and the carrying of small stocks enables small premises to be taken in any suitable town thus effecting a considerable saving in rent charges. Selling at uniform prices creates confidence in the minds of the buying public.

Disadvantages. Individual enterprise on the part of managers tends to be discouraged and there is little scope for exceptional ability. Where the demand of the public changes, large losses may be sustained in the carrying of huge stocks at the central depot of goods no longer required and for which the market is practically gone. Strict supervision of branches must be maintained by the employment of branch inspectors. Peculiarities in local or individual demand cannot be catered for where uniformity is established. As the work in branches becomes of a routine nature cheap labour is employed and little scope for ambition exists.

Departmental Stores *versus* Multiple Shops

From the point of view of organisation a departmental store may be distinguished from multiple shops in the following respects :—

1. The idea of a departmental store is to act as a universal provider; it tries to supply every possible need of the customer. But the chief idea of the multiple shop system is specialisation. The multiple shops specialise in a limited range of merchandise which appeal to customers.
2. In the case of a departmental store the site and premises are the chief

consideration. They are selected with care and they occupy a central position in the busy quarters of a town. The central position is not the chief idea in the case of multiple shops. It is sufficient if a multiple shop has a number of clients to give enough business. It may be situated in an obscure street.

3. In a departmental stores customers are pulled to the shop, in multiple shop system it is the shop which goes to the customer.

4. A departmental stores caters for rich customers who care for service and quality rather than for the price, but a multiple shop caters for the masses by offering its goods at a relatively cheaper price.

5. A departmental stores puts all its eggs in one basket, its whole success depending upon the continued prosperity of a definite geographical site. In the case of multiple shops, some may be successful, a few may be failures, and it is easy to cut losses by closing the unsuccessful shops and opening new ones.

6. A departmental stores may offer credit facilities and facilities for mail order business, but such services are not rendered by multiple shops.

7. A departmental stores has to maintain huge stocks of great variety and therefore needs a large amount of capital. In the case of multiple shops small stocks are enough and they can be replenished, if need be, from other shops at short notice.

Imp.

Mail Order Business

Mail order trading may be briefly described from the buyer's point of view as 'shopping by post'. It appeals to the public largely on the score of convenience. A mail order business is a business conducted entirely or mainly by means of the post, the goods being supplied direct to the customer instead of through any middleman. In mail order trading the medium of sale is usually a printed message which may be an announcement either in the press or by letter sent through post, whichever may be suitable in particular circumstances. The appeal to the customer is to be made, not face to face, but through print.

The causes of the development of mail order trading are many. One of them and the greatest is the realisation of the possibilities of advertising. Another is the rising standards of living which result in a demand among villagers for many things that they cannot always buy in local shops. Not long ago almost any manufacturer could obtain dealers' cooperation for his products; nowadays the dealers are often averse to pushing new goods and therefore the manufacturer finds it necessary or expedient to seek his own market. Mail order selling is, therefore, partly the result of the manufacturer's necessity and partly the result of a marketing policy dictated by expediency. Naturally the possibilities of the system are greatest in districts where there are few large towns or where shopping facilities are limited. In outlying districts certain articles are not readily available without sending to a large town for them, and it is here that the mail order trader has his best opportunity.

Convenience of the customer and profitable selling on the part of the mail order house are two chief considerations. Cheap price is also a consideration

which persuades one to go in for an article which may not always be of immediate need. People are educated and prompted to buy the goods offered for sale through the mail order system. The customer will naturally verify the price in the local market and if he finds that the article is not available in the local market for a lower price, you are certainly serving his convenience. Besides no business can justify itself unless it shows tangible profits. Profits can be earned only if you give the public an exceptional service—offering them goods at a lower price or those which they cannot get locally. It is this service which attracts a response from the customers and makes mail order business profitable. In the case of special goods not locally available a profit is a certainty, and thus it depends more upon the selection of articles. Nevertheless the convenience of the customers must always be kept in view. Confidence of complete service in the buyer is another requisite for success. You ask people to buy from a firm about which they never heard before, you ask them to pay the price in advance before they have an opportunity of looking at the articles. A customer has reason to doubt whether he would be able to get his money's worth. Confidence, therefore, must be inspired in the customers by offering the refund of the price of goods as well as postage incurred in despatching same if they are not found satisfactory.

In mail order trading articles are to be sold by advertising or circularising, to be despatched by post or by rail, to be sold to persons who have no opportunity of inspecting them, and the purchasers are induced only by a description of the goods. It is obvious that not all goods are suitable for mail order business. For example, sports goods, coloured textiles or bulky furniture are not suitable for mail order trading. Mail order articles should be such as can be understood fully from description, as can be easily selected from different models, as are capable of being delivered ready for immediate use, as are free from liability to damage in transit and are free from transport difficulty, and as lend themselves to pictorial representation and forceful descriptive writing. Novelty goods, chemicals and medical preparations, children's requirements, footwear and leather goods, jewellery, etc., give a good field for such business.

Fixing a proper selling price for goods offered through post is rather difficult. We cannot fix a very low-price because with cheapness people will naturally associate low quality. Prices are a strong point and they should be quoted in such a manner that the prospective customers feel that they are very low. The mail order business is made possible by the post office V.P.P. system, which however, does not permit of the parcel being opened for inspection before payment. Orders are secured by publicity in the press or by the distribution of circulars, handbills, catalogues, price lists, pamphlets, patterns, samples, etc. In some cases travellers are employed to visit previous customers, or there may be house-to-house canvassers. Catalogues and price lists are sent at intervals to regular customers. Once a correspondence is opened with a prospective customer it is followed up by an attempt to remain in constant touch

with him. A list of all prospective customers is prepared to which constant additions are made from time to time. This list is known as the mailing list. The mailing list, after necessarily allowing for a certain inescapable percentage of wastage, should comprise a bulk of prospects. Among the usual sources are directories, telephone guides, etc. A good way is to insert a small advertisement in prominent papers inviting inquiries on attractive offers. These replies would form the basis of the list. Similar repeat advertisements would add to the list and your experience and common sense would enable to eliminate the duds. You run a risk of some wastage because there is a percentage of negative results, but it is nevertheless worth while.

The catalogue should be of convenient size both for packing and postage. It is usually a work of art in the form of a folder. Its got-up and types are the last work in custom collecting technique. The classified lists inside the folder are arranged and displayed intelligently. The best folders append to each variety of goods their quality, cheapness or novelty. Continue to tap distant customers by follow-up in good letters inviting a trial order. Your judgment, experience, and your resources should be your guide. It is in the catalogue that the advertiser has more space to tell his story, it offers the good salesman his opportunity. The skill of a salesman, the gift of expression and descriptive writing, a knowledge of printing and illustration processes are all essential. There should be no niggardly saving of expense in production, paper, printing, illustrations and display, all of which should be of the best where a good article is concerned.

In no other business is a thorough system of office working so vital as in the mail order business, the reason being that results are so largely dependent on the keeping of inquiries and following them up, keeping in touch with old customers by correspondence, the necessity of tabulating statistics to test the results of advertising, and lastly on punctuality in dealing with customers' orders and inquiries. Proper card index records should be kept. The new cards should not only show the various transactions with the customers but they should also have a note of a customer's likes and dislikes and every bit of personal information relating to him.

Mail order business requires a high order of salesmanship. The mail order salesman must have the ability to describe clearly, definitely but briefly the nature of the articles, must be able to create interest and arouse curiosity and set out some inducement that will make the reader say "I think I want that". To create the desire to buy is the first step, sustained effort to convert the desire into actual order is the aim of what is known as follow-up system. There may be two advertisements of two similar articles. One may leave you cold and indifferent, while the other seems to breathe the breath of life; while one is featureless, the other is full of suggestive ideas and phrases that set you thinking. A person, if he has the skill, can use the words as the painter uses his brush; he can make you see things with the inward eye as he

would wish you to see them. The mail order trader, therefore, has to experiment with different types of copy. A responsive clue has to be struck. The mail order advertiser has no place to attract business; his business must stand or fall on the advertisement of a particular article.

Advantages and Disadvantages to Seller. Wherever the mail goes, there the printing advertising matter and the goods sent by the mail order house can also go. Through illustrated catalogues the customer is enabled to select his goods from a large stock. As the business is almost always done on a cash basis, economy is secured by the elimination of bad debts and collection charges. The overhead expenses are low since salesmen's salaries and expensive shop-fronts are not necessary, but this is partly offset by the cost of printing and distributing catalogues, etc. Advertising can be carried out more efficiently because results can be checked more accurately. The manufacturer mail order trader is independent of wholesaler and retailer; the substantial discounts that would otherwise have been given to middlemen are free to be used in advertising. The methods of mail order business are to a large extent creative in the sense that many unsuspected and untapped markets are discovered.

Customers demand not only low price but also service. The mail order trader falls short here and can never hope to supply it. However illustrated the catalogue may be, it cannot be as satisfactory as the personal inspection of the goods. Customers generally cannot be given credit facilities and that is a discouragement to many of them. Personal attention cannot be given to the likes and dislikes of customers. The sales appeal is stereotyped and cannot easily be varied to suit different types of prospective customers, and it is not easy to ascertain the causes of failure to effect sales.

Advantages and Disadvantages to Customer. The customer is enabled to get his articles at his own house and is saved of the trouble of going to the retailer. Many articles are available to the customer at his house at lower prices which are not either available locally at all or are available only at high prices. The customer gets more efficient service and sometimes buys better goods at cheaper prices. In the case of well-known articles there is no danger of wrong goods or goods of inferior quality.

People do not know with whom they are dealing when ordering by post. Sometimes the advertisements give a false idea of the quality of goods offered. The wording may be misleading; anyway it is not easy to ascertain the true quality. A customer has no opportunity of inspecting the goods he is going to buy. He cannot have immediate delivery; there may be annoying delays. Customers cannot enjoy credit facilities.

Hire-Purchase Trading

The hire-purchase system is the method by which the vendor agrees to supply goods to another person in consideration of that person agreeing to pay the purchase price by a stated number of payments of fixed sums at regular

intervals. To buy on the hire-purchase system is really to hire the goods, the instalments paid being in the nature of rent payable until such time as the total prescribed instalments are paid, the goods then becoming the property of the buyer. Until all the instalments are paid, the goods sold remain legally the property of the seller. This system of trading is making rapid strides, it has extended to a great variety of articles, e.g., furniture, radios, motor cars, typewriters, bicycles, gramophones, etc.

Besides the firms which specialise in selling to the general public on the hire-purchase system, almost all the large stores are ready to sell goods on the "buy out of income" principle. The price charged for goods sold under the hire-purchase plan are always a little more than the price for cash paid down, the excess representing interest for the period of credit granted. The supplier in this system does for the individual consumer what the wholesaler does for the retailer with scanty capital at his command. He makes good to the consumer his present deficiency of funds by supplying the goods on terms that permit of the buyer's saving out of future income the money with which to pay. Just as the slow-paying retailer suffers a loss of discount for using his creditor's capital, so the hire-purchaser has to pay a little more in price for the seller's advancing to him the whole of the goods before the buyer has had time to save their value.

As the seller retains property in the goods sold under the hire-purchase system until completion of the payments, fire insurance of furniture and similar articles sold may be required by the seller, whether this is provided for in the selling price or paid for separately by the purchaser. In most cases hire-purchasers are required to produce two sureties at the time of entering into the hire-purchase agreement. Sometimes the insurance of the purchaser's life may be required by the seller as security until the last payment is made. The hire-purchase system does not provide sufficiently for emergencies in which payments cannot be kept up, and the buyer is faced with the probability of a loss that he cannot afford to bear, should the arrangement have to be abandoned. What is a risky venture when taken for a necessity becomes folly when it is taken for a luxury.

The hire-purchase system originated in America and is very common in that country, the reason being that the mass production there needs mass demand, and mass demand for articles on the margin of the people's means needs inducements of every kind to move the ordinary person to buy. The desire to possess is stirred and encouraged and forced to big proportions by innumerable canvassers trained scientifically in the wiles of persuasive selling. For necessities such as a house and some furniture or for productive assets such as sewing machines or typewriters with which one may earn a living, the hire-purchase buying can be commended if the buyer's circumstances are favourable. In India the hire purchase system is still in its infancy on account of the low standard of living of the people and the absence of many traders who

are willing to sell under this plan. But with the improvement in the general standard of living the system is bound to grow.

Advantages and Disadvantages to Buyer. Immediate use of articles desired may be obtained instead of an indefinite period of waiting until sufficient money has been saved to make an outright purchase. Once an article has been acquired, money has to be saved to pay the instalments and it results in saving expenditure in other ways. If the article purchased is a luxury, alternative luxuries may have to be dispensed with, and there will be no temptation to spend the money on other less desirable articles. The alternative method of borrowing in order to make an immediate cash purchase is dangerous. The interest charged on such a loan will generally be higher than that paid under the hire-purchase agreement. So long as there remains a balance unpaid on the articles purchased the supplier will be much more willing than he would otherwise be to attend to any defects that may appear in the article afterwards. The system is of particular benefit in the case of capital goods, the acquisition of which will enable the producer to improve his methods of production earlier than would otherwise be the case; articles of this kind almost earn their cost before they are paid for.

A hire-purchase agreement is a mortgage on future income. Should unforeseen events alter one's financial position it may be impossible to maintain the payments regularly and the goods may be reclaimed by the seller. The first payment is high to cover the rapid depreciation of goods; hence if they are reclaimed the cost of hire for a short period will be disproportionate. The difference between the hire-purchase price and the cash price is considerable. The former includes sufficient interest and collection charges plus an amount to ensure the trader against bad debts. The balance of the purchaser's income after hire-purchase payments may not allow adequate saving to meet future liabilities. The making of compulsory payments at definite stated intervals may cause trouble and inconvenience.

Advantages and Disadvantages to Seller. A large increase in turnover generally results in profitable trading. With a properly worded hire-purchase agreement, the risk of loss will be small provided an adequate deposit or first payment is obtained. This must be sufficient to meet the difference between the price of new goods and value of immediately secondhand goods. Payments should not be spread over a longer period than the life of the article purchased. By a personal interview with the prospective hire-purchase customers and judicious inquiries at the time, the probable defaulters can be recognised and credit terms refused. In this way losses can be reduced to minimum. A connection with the customer can be maintained through his frequent visits which he would be making in order to pay the instalments. He may thus become interested in further purchases and some profitable business might be done. Additional capital may be obtained by transferring some of the hire-purchase agreements to some reputable finance company, the interest charged for such finance not being usually high.

A large capital is necessary to finance hire-purchase trading and unsound sales may lead to a large amount of bad debts. An expansion of hire-purchase business may result in the diminution of cash trade. The clerical organisation necessary for hire-purchase trading is intricate, troublesome and costly. A false position would be created if profit on hire-purchase sales is appropriated immediately. Even if the profit is spread over the years during which payments will be recovered, the income-tax assessment may be higher than the income actually earned. And necessity of reclaiming goods through defaults in payment will cause unpleasantness with the buying public, and this may lead to bad reputation.

The hire-purchase trading is not, however, so risky as it is imagined to be. There is a large body of respectable people who cannot buy things of value in any other way since they have only moderate means.

Instalment Payment System

The hire-purchase system has been modified by enterprising retailers, who, in order to offer further inducements to purchasers have evolved the system of instalment payments or deferred payments. Under this system the goods become the actual property of the buyer on the payment of the first instalment. It is the peculiarity of instalment trading that under it the article is sold outright and cannot therefore be returned, and the instalments must be paid. If the buyer finds it inconvenient to hold it, he can dispose of it at his discretion. But this cannot be done under the hire purchase system. In a hire-purchase transaction, the article being hired, the person possessing and using it cannot be its full owner until he has paid all the instalments. If he sells it without paying all these instalments he commits a criminal breach of trust and the original seller will have a right to recover the article from the sub-buyer.

Under the instalment payment system the seller has to take extra-ordinary risk in the shape of probable bad debts. So the prices charged are generally higher than those charged in case of hire-purchase system. The longer the period over which instalment payments are spread, the greater the percentage of expenses added to the cash price.

Under this system, a careful record has to be kept of the goods sold, of the dates when payments are due and of the actual payments made. A receipt is sent for each instalment and a final receipt when all instalments have been paid. For this purpose a card index is useful, each customer being allotted a card on which all particulars are entered.

The method of buying by instalments has its advantages and is economically sound provided it is not abused. People with small incomes find it almost impossible to pay cash down for the purchase of, say, an expensive wireless set or typewriter. And if they set themselves to save for that purpose, the period of waiting would be so long in most cases that they would probably fritter away their money in the meantime. By purchasing on the instalment payment plan,

the buyer is forced to save the money and the necessity of paying promptly imposes an additional incentive to save.

The system is of particular benefit in the case of capital goods or in the case of an article of lasting quality and utility, the acquisition of which will enable the purchaser to pay the instalment by earning.

The disadvantage of the system, however is that it frequently induces a person to mortgage his future income to an unhealthy extent. Therefore moderation should be the keynote in instalment buying.

The great advantage of the system is that it encourages trade.

But there are limitations in the way of successful instalment payment trading. In the first place, the instalment system can be successful only in case of persons whose credit and ability to pay are sufficiently well-known. As such it is mostly confined to persons with a fixed income. Secondly, there is possibility of the trader being too much reckless in the granting of credit, and unless proper care is taken, it will involve the whole trade in disaster. Thirdly, a large capital is necessary to finance this system and this may not be obtained easily.

Consumers' Cooperative Stores

Consumers organize themselves into cooperative societies to obtain their requirements of consumer goods and services on terms of greatest advantage to them and to secure for the small man many of the benefits of large-scale operations. This type of co-operation undertakes the retailing and wholesaling, and sometimes the production of consumer goods, and seeks to reduce trading costs by making buyers their own sellers. Unlike the producer movement which is concerned with particular classes of people in particular regions, the consumer movement carries an appeal to all persons because all of them are consumers, and may be regarded as an organization having the whole society for its membership. The movement is of particular interest to women as it enables them to make substantial economies in domestic expenditure.

Various plans were tried to eliminate the middlemen, but the one tried by the twenty-eight weavers of Rochdale was found to be the most successful. The Rochdale weavers were very poor, but were rich in the possession of four great virtues—courage, commonsense, patience and faith in effort. These are the qualities which ensure success in human endeavour. It was in 1844 that the twenty-eight weavers of Rochdale opened a small store with barely £28 as its working capital but with a great fund of zeal. How by the exercise of patience, perseverance and economy this small store helped the development of the present consumers' movement is a history of absorbing interest.

Most consumers' societies have been established on the principles first enunciated by the Rochdale pioneers. These principles advocate open membership, democratic control, cash trading at market prices, fixed return on capital and dividends on purchases. Open membership, democratic control and restriction on dividends are the basic ideas which lie at the foundation of all co-

operative societies. Cash trading has been adopted to avoid the risk involved in credit dealings, and sales at current market prices guard the society against business losses protect it from the charge of price-cutting, enable it to build up reserves and make the payment of dividends on purchases possible. These dividends are the rewards of saving through spending and provide the strongest inducement for membership and sustained loyalty.

Co-operative stores were organized in several parts of India almost as early as the co-operative credit movement. They did not, however, make any great progress until World War I, when the need for them was more keenly felt, and they increased in number and importance. The success achieved then was not retained, but World War II had given them a fresh and stronger impetus. Few rural stores and societies have so far been organized, and even in the province of Madras, where the consumer movement is strongest, only 400 rural societies have been established. At present the movement is largely urban. During the war, the rationing of foodstuffs and economic controls have been directly responsible for the organization of numerous small stores in cities and large towns since the Government have recognized them, wherever possible, as the distributive agency for the people. The middle and even the upper classes have, during the last two years or more, been drawn into these organizations. The commodities commonly retailed by urban societies are food grains, sugar, charcoal, butter ghee, cloth, etc., but the range of goods handled by them is widening and has been still more widened by their appointment as licensed sellers of rationed and other controlled commodities. The movement received a serious set back, during the last two years, with the introduction of decontrol policy, yet now with the reimposition of control it may be expected that it will receive an added impetus.

The main achievements of the consumer co-operative movement in other countries have been :—(1) Reduction in costs of retailing with advantages accruing to consumers, thus making possible more saving and higher standards of living, and contributing to economic stability. (2) Provision of better quality goods. (3) Promotion of thrift and consequent increase in economic security of members. (4) Education in intelligent buying, family budgeting, and general economies. (5) Better citizenship, the result of widely diffused ownership of an important democratic business enterprise. (6) Check on monopoly by co-operative competition and on profiteering.

The co-operative store movement in India may generally be described as a failure. A few stores here and there are being run successfully, but the success is due either to peculiar local conditions, as for instance, the absence of competition among the local shopkeepers, or to special facilities obtained, as for instance, lower railway freights and rent free quarters for the shops, as in the case of stores started by railway employees, or the college stores.

One of the main causes of the failure seems to be the ignorance of the basic principles of the store movement. Stores are generally considered to be

places where you can purchase articles cheaper than from a shopkeeper. The result of starting a store with such a notion is that the slightest setback damps the spirit of the members and destroys the sense of loyalty which is the backbone of success of such stores. The object of the store movement is to do away with the middlemen and ultimately to control the supply market as also the means of production on behalf not merely of the few members of any particular store, but of the whole community of consumers. Realising this principle the members of many stores in European countries readily pay even higher prices with the conviction that the temporary inconvenience will ultimately bring success to their cause.

Other causes of failure are the introduction of credit sales and the insistence on the part of members on door-to-door delivery by the store. It is the presence of these defects that account for the small number of cooperative stores in Japan. Though the number of other types of societies in that country is nearly 15,000 that of stores has not gone much above 150. Other causes which have brought about failure are the smaller margin of profit between wholesale and retail prices, and at the same time a high cost of upkeep. Dishonesty on the part of the manager is yet another factor; but this is found also in other branches of the movement as in the case of credit. It must, however, be borne in mind that no man is by nature dishonest; it is the opportunity that makes him so. If the Managing Committee were to keep a watchful eye, there would be fewer occasions for dishonesty.

An examination of the working of consumers societies all over the world shows that where there has been a failure it has been chiefly due to one or more of the following causes; lack of business training or ability or experience in the store personnel; want of careful study of members' requirements; stocking of goods that had only a limited demand because of the varied tastes of a heterogeneous membership; insufficient loyalty and interests among members; bad debts arising from credit trading; too narrow a margin between wholesale and retail prices defective methods of stock-keeping and accounting; and disproportionately heavy working costs. In India, in particular, two other important causes of failure have been too much dependence on honorary service and too small a size of the store to secure a competent staff and efficiency in management.

It may be emphasized that ultimately the cooperative consumer movement is to be based everywhere on independent societies functioning in each area, and that the difference in organization applies only to the initial stages, the difference being whether there should be independent units from the start or whether there should be a parent institution having branches, these branches forming the nuclei of future independent societies. While the former system which directly approaches the desired goal has been successfully adopted in Madras, there may be provinces such as Bombay where cooperative organizations are likely to fail unless full advantage is taken of the economies offered by

large-scale enterprise. In such cases, it may be suggested that the organization of consumer cooperatives should start with the establishment of a provincial society having branches spread over suitable regions with local members and local committees.

In provinces where conditions favour the adoption of the system of unitary organization it may be recommended that a consumers' society on the Rochdale principle should be established in each big village and town the aim being to have one society for a population of about 5,000. Funds needed by the societies to run their business will be drawn from their share capital and loans from central cooperative banks. For each group of about 50 conveniently situated urban consumers societies and rural societies dealing in stores, a central society should be organised, to which they should be affiliated and they should purchase a prescribed number of shares.

In those provinces in which the conditions are such as to require the establishment of a central organisation first, it may be recommended that a provincial consumers society should be established, which should as far as possible combine in itself the functions of the primary, central and provincial societies. As its business is established and its position stabilised it will gradually extend its services to other towns by opening branches. If the latter are ultimately to be converted into independent societies, which is our aim, it is necessary that the parent institution should allow, consistent with efficiency, the patrons of each locality to man a local branch and when sufficient local interest has been aroused, it should offer to the local patrons the option of converting the local institution into a society of their own.

2 Wholesale Trade

The wholesaler is a trader, who purchases goods in large quantities from the manufacturers and resells to retailers in small units. In point of fact, a true wholesaler is one, who is neither a manufacturer nor a retailer but acts merely as a link between the two—producer and consumer. We can picture the wholesale warehouse situated on the course of supply as a kind of reservoir, giving temporary storage to portions of the supply on their way from makers' works to retail dealers' shops.

As the wholesaler is a connecting link between the manufacturer on the one hand, and the retailer on the other, he renders valuable services to both the parties. Let us first examine as to how he helps the manufacturer.

Mass production and cheapness go hand in hand. The wholesaler places very large orders with the manufacturer, who produces goods in large quantities and thus enjoys the economies of large scale production. The wholesale merchant helps the manufacturer by placing a large order for each kind of goods to be made. He collects small orders from the retailers and classifies them into various categories and then places a big order with one manufacturer well-known in one type of goods, and another big order with the second producer and so on. Generally goods are produced in anticipation of demand. The wholesaler takes

upon himself the responsibility for holding stocks, and thus helps the manufacturer to carry on with much less capital than would be necessary, if the manufacturer had to lay out permanently large sums in stock as well as in costly machinery and holding the stock continuously against possible demands from the retailers. As the orders are big the wholesaler places them with the most efficient producers, who get sufficient orders to keep themselves engaged in that work only. Such an arrangement, of course, permits the manufacturer to specialise to some extent in the kind of goods he can produce best. Large orders lead to mass production and the latter in its turn leads to specialisation. The wholesaler studies public taste and fashions and directs the manufacturer as regards the quantity and quality of the goods to be produced. Retailers desire credit which, in the absence of wholesaler, should have been provided by the manufacturers. Much of the business between the wholesaler and manufacturer is prompt cash. The manufacturer is thus able to carry on his business with comparatively small capital. Ultimately the goods produced must be sold. Except, of course, in a few cases when the manufacturer sets up his own sales machinery, he is relieved from the art of selling as it is performed by the wholesalers. The manufacturers thus need not be expert sellers as they produce goods for orders.

The wholesaler renders the following services to the retailer. The retailer finds it convenient to obtain in the warehouse of the wholesaler many kinds of goods and many varieties of each kind, drawn from many makers. Had the wholesaler not been there the retailer of necessity had to wait for a long time to satisfy his demand, because in that case, the retailer will be required to place different orders with different manufacturers, which would mean great delay and expense. The retailer commands little capital and, therefore, cannot afford to invest it in varied stock. The wholesaler is an ever ready fountain of supply of goods. The policy of the successful retailer is to turn his stock over quickly, to hold at one time so much only of one kind of goods as will serve to meet his customers' wants for a short period, and to renew without delay any class of goods that he finds running out. The manufacturer cannot execute an order at short notice unless the goods for which an order has been placed are being produced in anticipation of demand. Still more important is the financial assistance given by the wholesalers to retailers in those trades where wholesalers regularly allow credit to their retail clients. The manufacturer cannot afford to grant credit to retailers. The wholesaler benefits the retailer in passing on to him some of the advantages of specialisation. The marketing function is performed by the wholesaler. Specialisation travels in both the directions. The retailer buys from the cheap wholesaler and the latter from the best and cheap manufacturer. Thus the retailer is benefited not only by his but also by his suppliers' experience. The wholesaler brings to the retailer the new types of goods for which a market has to be created. The wholesaler, being the controller of the supply, so to say, tries to maintain an equilibrium

between demand and supply. In other words, it is he who maintains the price level by expansion or contraction of the supply of goods, as the prices go high or come down respectively. The market price thus tends to oscillate near about the normal price. This regulation of price by controlling supplies minimises the risk of the retailers.

The wholesaler benefits the ordinary public as well. It would have been very difficult for the retailer to offer a better choice of goods in the absence of wholesalers. The retailer supplies to the public a fresher and most up-to-date stock of seasonal and perishable goods. As the manufacturers are enabled to specialize and produce in large quantities, the cost of production is lowered. The natural consequence of it is that retail prices are also reduced.

Eliminating the Wholesaler. The tendency towards elimination of intermediaries emanates from the ideas of cutting out the profits of middlemen. A very considerable margin exists between what the farmer receives for his milk or his potatoes and what the householder gives when these necessary commodities reach his door. Where does all this margin go? It is, of course, eaten up by a large chain of middlemen. Every link adds its quota to the price of the goods to cover expenses, wages, and profit, and these charges must be justified by the advantages resulting from the services rendered.

The reader may now quite justifiably ask, "Is the wholesale trader needed?" There are certainly strong forces operating to shorten the chain between manufacturers and consumers. In the first place, rapid communication, national newspaper advertising, the post office V. P. P. facilities have put many manufacturers in direct touch with the consumers. In the second place, the growth of multiple shops and departmental stores, has created vast retail organizations able to deal direct with manufacturers, and indeed to control them. In the third place, manufacturers in their turn have opened multiple shops for the sale of their products. In the fourth place, intensive advertising of "branded" goods has enabled the manufacturers to compel retailers to stock their goods and to deal direct with them. In the last place, the co-operative movement is largely independent of the wholesaler. Yet the middleman survives. What is the explanation of his survival?

The answer lies in the fact that the wholesalers' functions cannot in any case be eliminated and these functions are much wider than the activities of any one retailer or manufacturers. Under the present system it will never be possible for all retailers or all manufacturers to incorporate as part of their organisation departments doing the work of the wholesaler, and in only a few cases is it profitable for either the retailer or the manufacturer to attempt to do so. Moreover neither producer nor retailer is usually in a position to face the price changes arising from the fluctuations in the supply of goods.

The functions of the wholesalers are obviously important. In the main they are quite distinct from the technical problems of manufacturer and the commercial and psychological problems of retailing. The wholesaler undoubtedly permits

both the other parties to specialise to the greatest extent and helps to balance manufacturing and retailing, and hence to lessen the likelihood of mistakes in the anticipation of demand.

Whether or not it is advisable or profitable to eliminate the wholesaler is, therefore, a matter to be decided in each particular case. For small retailers and for producers of perishable goods particularly, the wholesaler is probably essential but in the case of the larger concerns he is probably an unnecessary link.

Site and Location. As the wholesaler deals exclusively with the retailers, the question of premises is not as important to him as to the retailer. Still, while selecting a site for the premises due consideration should be paid to its accessibility to trade customers and convenience for the delivery and despatch of the goods stocked by the wholesaler. Invariably, wholesale trade tends to be localised into certain parts of the city. Again, in case of a retailer, well-fitted premises are a necessity as he has to appeal to the individual taste. A wholesaler has to deal chiefly with the buyers from the retail shops, and can easily dispense with these attractions.

Purchase Policy. Buying commitments should be subject to strict supervision. The extent of the buying commitments is important, because sooner or later the goods will come in, and provision will have to be made to pay for them. In order to avoid over-buying attention should be paid to stocks in hand. It is bad business to hold more stock than the amount of turnover really warrants. To put it alternatively, care should be taken to avoid over-stocking. Stocktaking should be resorted to after periodical intervals. This will not only act as a check on over-buying but will also help the shop to avoid being out of stock. For there is nothing more harmful to trade than having to refuse goods which are asked for, with the excuse: "They are expected in tomorrow," or some such apology. The orders for the seasonal goods should be based on the trade done last season, with a careful estimate of prevailing conditions of trade and prospects of good or bad season. These data, as guides to the buying, can be ascertained either from the invoice files of a year ago or from Orders Outward Book. Unsystematic and careless buying results in overstocking, which tends directly to reduce the gross profit. It locks up capital unnecessarily, and may easily lead to the weakening of that credit which is inseparable from the good name of the business.

Receipt and Storage of Goods. The traders' functions can be arranged in a certain sequence something like this: buying, receiving, storing, showing and selling. Particular attention should, therefore, be paid to the carriage of goods, as carriage inwards is a part of the cost of goods. Now evidently, getting goods sent the cheapest as well as the safest will reduce costs. 'Safest' is said because, in the case of easily damaged goods, the cheapest way may not be the safest. The extra carriage to be paid on the "Company's Risk" will be in the nature of an insurance against loss in transit. On arrival the goods should be thoroughly examined. The system of receipt of goods should

be one, which should ensure that goods taken into stock are in good condition, that the quantity is right, and that charges, if any for carriage, etc., are correct.

Before any invoices are passed to the accounts department they should be thoroughly checked with regard to the quantity, quality, price calculations, etc. In the end, the buyer who is responsible for the order should examine the invoice and initial it to indicate its regularity. This is technically known as "passing the invoice." The invoice may now be passed to the accounts department for necessary entries. The invoice is finally filed away in the invoice file under its distinctive number so that it may be ready for reference at a moment's notice.

When the goods are received there must also be some system in the matter of storage on the premises. If a wholesaler is also a retailer, the warehouse may be a place of unbroken packages and the shop for the goods broken out from the boxes or packets. There should be a place for everything and everything in its place in the warehouse, cellar and indeed also in the shop. The goods should be so stored that they may be free from damage and goods first received may be first despatched i. e., the old stock should be brought forward for sale before the new is touched. It has been well said that "Order is the heaven's first law."

Sales Organisation. The wholesaler has two possible alternatives of approach to the customers—direct intercourse with the customers or indirectly by means of middlemen. Besides controlling the purchasing of his department each departmental manager is responsible for disposing of his goods at a profit. He should be given a fairly wide latitude in fixing his price. His remuneration should be based not on the sales but on the gross profits, for if the former basis were adopted there would be a tendency for the buyer to augment his sales by reducing the profit margin. If a complete system of budgetary control is in operation he will be required to furnish periodically estimates of his sales for subsequent periods.

Though display and window-dressing is not so important as in retail trade, yet the indoor salesman must function in a well-kept show room, where retailers may inspect the goods. The retailers do make periodical visits to the show rooms and give their orders then and there. Sitting accommodation and other facilities should be provided in the interest of business.

For his outdoor sales, the wholesaler depends mainly on his travellers, each of whom is usually allotted a closely defined district to canvass for sales. The traveller's job is not an easy one. His main consideration is not to push his sales but also to build up a satisfied clientele. His path is strewn with difficulties. He should also serve the customers by advising them of best methods of display, possibility of changes in fashion or design, likely demand of the products, etc. Besides keeping in touch with the existing customers, he must attend "dead" clients as well, who may very often be brought to life by attention to quite trivial matters. Ultimately his task is to canvass new customers.

Wholesale Advertising. Increasing sales should be the aim of every

trader. The best way to push sales is the traveller, who can emphasise the special selling points. The wholesaler's extensive and multifarious activities compel him to fall back upon advertising in trade journals and on direct mail advertising by issue of circulars, leaflets, catalogues and price lists. Such reminders despatched at regular intervals may be very useful in supporting the visits of travellers. Circulars must be prepared in the form of a personal letter. The extra expense of postage must not be grudged, and the method of duplication must be employed which has the resemblance of an individual letter. Invariably in big businesses one finds a Publicity Department which prepares price-lists, catalogues, leaflets, etc. In the wholesale trade, press advertising should be limited to selected trade journals, otherwise the expenses may be a risky investment.

"Branded" Goods. The wholesaler before resorting to advertising should get a figure or picture registered, which will be assigned to his goods, known as "Trade Mark" or "Brand" respectively. This will make known to the public that those goods are manufactured or sold by a particular trader. The advantages claimed on behalf of such a registration are: Special demand can be created for such goods. The price can be fixed by the producer in the interest of the consumers. The manufacturer, to maintain his good name, does not lower the quality. Once confidence is created in the public, the cost of selling goes down considerably. Sometimes the wholesaler may be dispensed with. Both the wholesaler as well as the retailers are benefited by this form of publicity. The retailer is assured, more or less, of a established demand. The quality too can be standardised. The disadvantages, however, are that the retailer has to sell goods at a fixed price and that he may not be allowed to sell other goods of a similar type.

Complaints. Is the customer always right? Some would say 'Yes', while others would go to the other extreme end. The arguments of one who replied in the affirmative may briefly be stated as follows :—

The customer alone knows exactly what is wanted and the purpose to which an article is put. If the customer declares that the price is too high or that a similar article at a lower price can be obtained elsewhere, he must be regarded as right. A friendly inquiry about the price the customer is prepared to pay, and of the prices charged by the competitors give proof of an intelligent business interest. Where any complaints about quality or durability of goods purchased are made, the customer is definitely right. It is useless to pass on the blame to the manufacturer; this merely proves bad buying on the part of the firm. Replace the goods or offer a cash refund as an indication of good faith.

The antagonists, as a matter of course, cannot see eye to eye with their opponents. Their arguments may be put forth as under :—The customer cannot be expected, in the majority of cases, to know nearly as much about merchandize as the salesman, who should be a specialist. Any criticism is

therefore, probably due to ignorance. Where the price is stated to be too high, some possible substitute at a lower price should be offered. Customer's declarations about competitive prices are usually erroneous, the difference in price being due in most cases to differences in quality. Cheaper grades must, therefore, be introduced to meet the requirements of the cheap customers. If the complaints about quality and durability are the result of unreasonable expectations on the customer's part, the superior merit of high priced articles should be pointed out.

If any complaint is lodged by the customer it should receive minute attention of the higher authorities. The letter must be immediately replied to in a polite tone and assurance should be given for the non-repetition of such a mistake. It will be better to pay something by way of compensation to the customer, and to keep him satisfied, rather than to leave his custom. To conclude, therefore, a satisfied customer is the best advertisement a firm can have. A small loss borne in giving satisfaction is a permanent investment that will yield limitless dividends.

Control of Credit and Collection. Credit sales are predominant in the wholesale trade for two reasons. Firstly the average size of an order in the wholesale trade is considerably larger and not infrequently the order may extend over various departments, and if the sales were made on the cash basis, the buyer before he could settle up, would have to wait for the receipt and the invoice. Thus time is saved. A customer usually has to make frequent purchases from the wholesaler. If each of these were to be settled for cash there would be considerable waste of time and labour. Hence it is usual for the wholesaler to render his customer's accounts at regular intervals and for payment thereof to be made in one lump sum. Moreover, arrangement may be made between the wholesaler and the retailer that the latter would pay his account within a stipulated period and shall receive cash discount if payment is made during that time.

As in the case of stock, so in the case of book debts there are two points at which credit must be carefully watched: (1) on the granting of credit—to make sure that credit is not given in quarters where it will be abused, (2) when accounts pass the due date without being paid—to prevent them from remaining overdue any longer than can be helped. The preparation of *Total Debtors' Account* at the end of each month may be very helpful in this case.

The next point is how inquiries about new customers are to be made. In the first place, the wholesaler can write to a business friend, who lives in the same town to which the prospective customer belongs. This is probably the easiest and the best. In the second place, he may ask the would-be purchaser to mention the names of at least two referees from whom an enquiry may be made. This method is most common. In the third place a reference may be made to the bankers of the would-be customer. In the fourth place, if the prospective customer is a member of a trade association, it may throw light

on the financial standing of its member. This kind of inquiry is limited only to the members of the association. In the fifth place, in the industrially advanced countries there are professional undertakings which devote themselves to the supply of credit information, in return for a certain remuneration and are known as Information Bureaus.

It is a wise policy to be pursued not to open accounts without the specific authority of the credit department. It is necessary to see that the account opened is only operated upon within the limitations authorised. This, of course, involves the limitation of credit authorised being communicated to the ledger clerk. The limit both as to amount and as to time would be stated at the head of the ledger account.

It is a good plan to arrange that each ledger clerk shall, as a matter of course, report all overdue accounts to some prescribed authority. As soon as the accounts become overdue a written application for payment should be made. If the account remains unpaid in spite of repeated applications, some more drastic steps must clearly be adopted.

Control of Cash. The precautions that may be adopted by the proprietor of a business to guard against misappropriation of cash by the cashier are as follows :—

The cashier should not be allowed to have access to the ledgers or books of prime entry. All correspondence should be opened by a responsible official and cheques and postal orders received should be crossed especially and marked 'Not Negotiable' and entered in a rough cash book or cash diary by a clerk in attendance, which should be checked and initialled by both the official and the clerk. The remittances should then be passed over to the cashier who should prepare counterfoil or carbon copy receipts which should be signed by a responsible official before despatch to the customers. The unused stock of receipt books should be kept under lock and key. The cashier should make entries in his cash book from the receipt book; should fill in the pay-in-book and bank the entire cash every day. There should be a sound method of recording and checking each sale. If travellers are allowed to collect book debts, they should be subject to proper supervision. All payments save those for small amounts should be made by crossed cheques. All invoices and statements received from creditors should be checked and initialled by those responsible for checking them. Every payment should be passed by a responsible official before a cheque is drawn, and at the time of signing cheques the official should see that the payment is in order. A sound system of internal check should be in force in connection with the payment of wages. Vouchers received for payments made should be examined with the Cash Book, and should be properly numbered and filed. The Pass book should be periodically checked and reconciled with the Cash Book. At irregular intervals, the balance of cash in hand should be counted by a responsible official.

Control of Expenditure. For the successful running of a business

preparation of returns and computation of tables and statistics with regard to purchases, sales, stocks, expenses, etc., is indispensable. The tables can also be represented by means of diagrams and graphs. In some ways presentation of statistics by graph is more striking than presentation in tabulated form. The system of returns and reports, in any large concern, forms part of an organised system of Budgetary Control or scientific financial management, which involves the setting up of a standard for every measurable commercial and industrial activity, with a view to ensuring that the programme of each department is entirely adjusted to the policy of the business. In this way, departmental heads are tied down to the exact statement of what they can do on the basis of an agreed policy. The first step to be taken while introducing Budgetary Control is to estimate the volume of sales for the period (say one year). Such a forecasting requires an exhaustive analysis of every element entering into the market conditions and will probably raise many problems which were previously unnoticed. The programme and expenses of each department are then determined on the basis of sales quota. The advertising expenses are also allocated, the cost of purchasing and production expenses on the given figures are estimated, and, expenditure on rent, rates and taxes, office and distribution for the period is calculated. These figures will show whether the estimated volume of business is likely to cover expenses and how far it is safe to lower down the price. Budgetary control, however does not end here. It requires that periodical reports should be prepared showing how actual results compare with the estimate, and these should be submitted to the Budgetary Controller, who is generally the accountant. Thus the control of purchases, sales, stocks, book debts and of presenting periodical statements to the management is an application of budgetary control.

Test Questions

1. It is said that the cost of retail services is very high today. Do you agree? Could you suggest a way by which the cost could be lowered?
(Bombay B. Com. 1941).
2. Analyse the factors which influence the efficiency of a retail organisation.
(Bombay B. Com 1942).
3. Why is a large-scale retail organisation more efficient than a small-scale one?
(Bombay B. Com 1942).
4. Why is the efficiency of management greater in large firms than in small firms? If large-scale management is more efficient, how do you account for the existence of a number of small firms?
(Bombay B. Com. 1941).
5. Briefly describe the various forms of large-scale business which have become prominent in retail trade. What has been the effect of the increase of Multiple shops?
(Allahabad B. Com. 1936).
6. How would you organize a departmental store? Discuss its prospects in India.
(Allahabad B. Com. 1910).
7. What causes have led to the growth of the Multiple Shop system in

the retail business? How is it that this system has not so far developed much in India?

(Allahabad B. Com. 1937).

8. Distinguish between (a) Multiple shops and departmental stores; (b) Hire-purchase and deferred payment systems.

(Bombay B. Com. 1947).

9. Give the advantages and disadvantages of hire-purchase trading from the point of view of (a) buyers, and (b) sellers.

(Agra B. Com. 1944).

10. What is instalment selling? How does it differ from the hire-purchase system? Do they help to increase sales?

(Bombay B. Com. 1945).

11. The owner of a small retail shop finds his business declining due to the opening of a branch of a multiple shop organisation in his neighbourhood. What steps would you advise him to take?

(Bombay B. Com. 1942).

12. What services are rendered by wholesalers to retailers? Should the wholesalers be eliminated?

(Bombay B. Com. 1947).

13. Outline briefly the organisation and describe the functions of the purchase department of a commercial firm. What are the advantages and disadvantages of large-scale buying?

(Bombay B. Com. 1941).

14. Why do manufacturers usually prefer to entrust the marketing of their products to a separate organisation?

(Bombay B. Com. 1935).

15. Outline briefly the organisation and describe the functions of the Credit Department of a commercial firm. What methods are available for co-ordinating the activities of the Credit Department with the work of the Sales Department?

(Bombay B. Com. 1940).

16. Outline briefly the organisation of a sales Department. Is a larger sales Organisation more efficient than a smaller one?

(Bombay B. Com. 1939).

17. Describe the internal organisation of an Indian wholesale firm engaged in any distributive trade.

(Agra B. Com. 1946).

18. As the general manager of a large wholesale firm, what system of internal organisation would you introduce with a view to preventing the misappropriation of cash?

(Agra B. Com. 1945).

19. What are the chief characteristics of a mail-order business? Can it be a successful agency for retailing agricultural goods in India?

(Agra B. Com. 1948).

20. What are the various difficulties in the way of the adoption of the hire-purchase system in India?

(Bombay B. Com. 1935).

21. What attractions does the hire-purchase system offer to the purchasers? Describe the features essential to an article suitable for hire-purchase business.

(Bombay B. Com. 1935).

22. Discuss the relative advantages and disadvantages of being a customer of (a) a large department store; (b) a small retail shop-keeper; and (c) a co-operative distributive society.

(Bombay B. Com. 1938).

23. What advantages does a large retail store, like a departmental store or a chain store, enjoy over a small retailer? Do you think such a store has any future in India?

(Agra B. Com. 1947).

CHAPTER 7

BUSINESS COMBINATION

The outlook of the 19th century upon the economic order was increasingly dominated by the view that supplies, prices, profits and wages were best left to look after themselves. Let the State give no privileges and set no impediments, let it leave the business world to its own devices, and the natural law would ensure that all would be for the best. The desire for gain would urge each to maximum effort, and competition would harmonise supplies and requirements, would ensure that the level of wages, prices and profits were about what they ought to be, and would make for the elimination of the less fit economic unit and the survival of the more fit.

What was not sufficiently realised by those who believed in the above law of competition was that the law will freely operate only where a condition of perfect economic freedom prevails and that it will operate to best purpose only when buyers and sellers have the widest knowledge of present and prospective demands, supplies and prices. A condition of economic freedom demands something more than non-interference on the part of the State, it demands the unimpeded access of all buyers to all sellers and the absence of all action in restraint of free competition on the part of those engaged in industry. At no time has such a condition prevailed over the whole industry and trade. It was probably most nearly reached in the first half of the 19th century when, following upon the great inventions, the improvement in transport, and the extension of joint stock financing, new enterprises sprang up and offered their wares with a minimum of collusion over extensive areas, but even then economic freedom was far from perfect, and it was to become steadily less so. In the last quarter of the 19th century a new law began to force itself on the attention of the economic world; the law that *"competition begets combination"*. However confidently it may be asserted that competition is only human nature, it is not in human nature that two, or ten, sellers should go on undercutting each other to the advantage of buyers when by agreement between themselves they can establish a common fair price or control the common output and so keep prices above the competitive level. It is this second law that has already come to engage the attention of governments in many countries and is likely to constitute one of the major problems of government for many generations to come.

Nonetheless, competition still prevails over wide areas of trade and in examining the nature and governance of demand, supply and price, it is still most convenient to assume free competition and then to enquire into the extent

to which the limitation of competition by external circumstances or by the deliberate action of interested parties nullifies the conclusions reached,

There comes, however, a stage at which the continuance of competition along the old lines is actually detrimental to industrial efficiency. Aggressive competition expends effort which might much more beneficially be given to improving and cheapening method, process and product. Undercutting among rival manufacturers may lead to goods being sold at cut-throat prices, but the price may nonetheless be higher than it might be if the individual firms were in friendly communication or if the manufacturers were concentrated in a few, instead of being spread over many, establishments. Competitive production often means a wasteful duplication of activity and plant. When such a stage is reached or when industrialists wake up to the fact that there is an easier way than competition to the ends they pursue, competition gives place to combination.

Causes of Combination Movement. The various causes that brought the combination movement into being may be stated as follows :—

1. Towards the end of the 19th century there was a marked decrease in the opportunity for speculative gains along the old lines. Formerly there had been a wide field of natural resources to be exploited, but this field had been narrowed down. Consequently the old opportunities for great gains through exploiting such fields rapidly diminished. This fact, when coupled with the desire for gain through the employment of a large amount of capital and a multiplied labour force, impelled industrial leaders to seek new fields such as existed in control of manufacturing industry through combination.

2. A development in the character of markets and business risks came to a head. Markets became world-wide and business risks were increasing. Hence the way to control the business situation and reduce the risks of exchanges was to combine the direction and management of the various producers.

3. The most important cause was the increasing severity of competition. With modern large-scale capitalistic production, competition often becomes cut-throat and intensely wasteful. Transportation developments also increased the intensity of competition by building up larger business units and then adding to the force of the clash between them. The severity of competition was increased by the fall in general prices which took place at the end of the 19th century.

4. The desire to secure potential gains by regulating prices and trade conditions encouraged combinations. More particularly characteristic of the time, however, was an almost conscious realisation of the possibilities of profit on a large-scale production of the common necessities of life. Captains of industry arose who saw, first, that great profits might be made by selling large quantities of such products even at a small profit per unit, and secondly that in selling such things monopoly would have great power because the demand for them does not fall off rapidly when prices are raised.

5. The tariff facilitated this movement by raising a wall against foreign competition. Once protection is granted to an industry the outside competition disappears and forces are at once set in motion which encourage combination in that industry.

6. The development of joint stock enterprise was itself a factor in facilitating combinations. Through the agency of joint stock shares the control over a large number of business organisations may readily be concentrated in the hands of a few men.

7. When businesses tends to increase in size, there is a decrease in the number of competitors, but competition becomes keener. Under the old conditions personal element and customary scruples held considerable sway, but under the stress of competition productive economies are squandered partly in advertising, etc., and partly in the form of cheaper prices. The intensity of competition thus generated under developed capitalism drives the competitors to seek some arrangement with one another.

8. The combination movement can be partly accounted for by industrial and technical conditions. Modern technique demands large scale enterprise and consequently favours combination. There are other reasons, however, which, if they do not initiate, speeded up this natural process and were most apparent in the economic conditions of different countries which prevailed after the World War I.

Maldistribution and dislocation of industry were caused by the war in all countries which participated in it, but the effect of this dislocation was not alleviated but aggravated by the peace treaties. Larger economic entities were broken up; a number of new states were created; economic nationalism of the worst kind made its appearance everywhere, industrial areas turned to agriculture, agricultural countries built up industries with little or no regard to productivity or industrial efficiency, and tariff walls were erected. Overstocking of raw materials in agricultural lands and of manufactured goods in industrial countries, chronic unemployment, and a large destruction of fixed capital were everywhere the consequence. It is but natural that under these conditions European industry turned to form combinations as its sole effective remedy.

Another phenomenon after the last war that intensified the combination movement was the great attention paid to rationalisation in the post-war years. All the leading industrial countries have made serious attempts to rationalise their industries, and the combination movement is one aspect of rationalisation. Most of the economies contemplated under rationalisation cannot be effected by small business units or in individual enterprises. In the face of hard postwar competition with increased production and dwindling overseas markets, all were hard pressed to reduce their cost of production and to be able to keep their heads above water. There was a run for safety and this combination movement was one of those safety devices which enabled them to have some economies of large-scale production.

Forms of Combination. The regulative as distinct from the purely competitive principle of trade and production has an ancient and historic origin. Joseph, as corn controller of Egypt was representing a powerful food combine which affected a substantial portion of the then known world. The ancient guilds in Great Britain and the Continent of Europe controlled industry and trade, in their then very limited sphere, by regulation and coöperation, thus restraining competition. Today the small manufacturer or trader who increases the number of his establishments simply applies in a limited degree the idea of combination. By utilising his own directive force and initiative over an extended area of trade he hopes for an expansion of turnover and profits without increasing his prices.

Thus, through history, commerce and industry have been shared and governed by free competition on the one hand, and by regulation and combination on the other. That is equally true of modern private and capitalistic enterprise. Combinations are known by different names according to the form they assume, such as conventions, rings, corners, cartels, syndicates, combines and trusts. They may however, be divided into two main forms, namely, (i) Cartels or Associations, and (ii) Trusts or Combines. A fixed meaning cannot be applied to either of these terms and frequently they are used interchangeably. The transitions from one type to the other are frequent and take place in a variety of ways. Hence it is better to refer to different combinations as of certain types, according as they most resemble the cartel form or that of the combine.

The Cartel or Association

A cartel is an association of independent undertakings in the same or similar branches of industry established with a view to improving conditions of production and sale. They are called 'syndicates' where they have set up a common sales organisation. Cartels are frequently national or even international in character.

The cartel is a looser form of industrial combination and it allows the different businesses joining the combination to retain a substantial amount of individuality and liberty. It does not directly control the management of the different businesses joining it and it does not fix a uniform rate of profit for all those businesses; it generally fixes only uniform selling price for the commodity produced by the different businesses and it also regulates their output. With its looser organisation it can be more easily formed and more easily dissolved. The cartel system prevails largely in Germany, Austria, Belgium and other countries of the European continent. Some of the powerful cartels are to be found in the pig iron, steel and manufactured metal trades in Germany and Austria.

Cartels have with some amount of justification been called the "children of distress." Unrestricted competition has often led to an intolerable state of affairs or even to the complete ruin of competing enterprises. Such compe-

tion is not always one of prices, but sometimes has reference to quality or terms of payment, and often leads to the unrestricted production by the single business and the flooding of the market with unsaleable goods. There is only one means by which such a drawback can be overcome, viz., an agreement among the competitors themselves. Like exhausted parties in a war, they conclude peace by handing over to a central depot the weapons of competition, such as the fixing of the sale price, the quantity of output, etc. As a matter of fact most cartels have originated in times of crisis or of distress in certain branches of industry.

Forms of Cartels. The different forms of cartels are those which are concerned with business conditions, price regulation, quota fixing, and the regulation of markets.

Business Conditions. Co-operation is extensively directed to the purpose of regulating conditions of sale, especially in relation to conditions of delivery and of payment.

Price Regulation. A more advanced type of cartel is that which has as its basis an agreement governing selling prices. To simplify control it is necessary to set up a central sale office serving the joint interest of members.

Owing to the existence of low-cost producers and high-cost producers in every industry, the tendency is to fix the level of prices beneficially for the high-cost producers. This inevitably antagonises consumers and also attracts outside competition. Furthermore, the low-cost producers are unlikely to be satisfied, even with the higher rate of profit, because they have sacrificed their competitive power for the benefit of those less well situated. Any pressure of outside competition usually results in the secret breaking of the price agreement by means of rebates or other inducements.

Quota-Fixing. To overcome the obvious disadvantages of the price-fixing cartel, it is usual in international industrial agreements to introduce a "quota" system which either divides the total sales between members, or fixes the quantities which members are allowed to produce. Such arrangements involve the creation of effective supervision, which may take the form of a central company to which members supply the required information, or there may be established an organisation which receives orders and distributes them to members according to their respective quotas.

The most complete cartel organisation has a separate company which operates as a central sales office for the members, and sells the entire production for their joint account. It is not uncommon for such quota cartels to allow members to produce in excess of their quotas, subject to the payment of compensation into a common fund for the benefit of the other members.

Regulation of Markets. An alternative to the quota system based upon production or sales is the "territorial" cartel which has as its basis the allocation of markets amongst its members.

In many cases cartels embody the principles of more than one of the above

mentioned types, whilst practically all will require to introduce the simple first type of regulating conditions of sale.

Much of the criticism against cartels is due to the secrecy which surrounds their formation and the lack of publicity relating to their activities. Consumers are kept in ignorance of the policies which direct them, and are in consequence unable to judge whether in the long run the working of the cartel will be to their advantage. It is a common belief that when an industry is controlled by a price or production cartel, the incentive is removed for the advancement of manufacturing methods. This view does not take into account the constant desire of cartel manufacturers to increase their profits, and because the volume of production and the price and conditions of sale are controlled, the only possible way of doing this lies in the direction of improving efficiency, and thereby reducing costs. The tendency, therefore, is for cartollised industries to adopt the most up-to-date technical improvements both to reduce costs and to improve the quality of the products.

In other ways too a cartel can achieve important benefits, both for its members and consumers. Economies can be effected in research work, in trading costs and in publicity expenditure. Considerable savings can also be made in distribution by the elimination of unnecessary transportation costs. Given the higher development of cartel administration in conjunction with a moderate price policy aimed at increasing consumption, there is good reason for consumers to regard cartels as beneficial to their interests.

The Economic Policy of Cartels. The economic policy of cartels is guided by the desire to effect with united forces a satisfactory sale of goods or services for their members. The aim is to control as far as possible the supply of the goods so that prices may be regulated. During the period prior to the establishment of a cartel, competition among the undertakings leads to such a depression of prices that an improvement can be expected only by a restriction of competition. The cartel aims at securing this restriction, but in its lowest stages of development it does not completely attain this end. There are always loopholes which cause internal competition to become active or which render possible outside competition. Not until a higher stage is reached does the cartel become a weapon for influencing prices, for the regulation of the turnover, and finally for the regulation of the output.

Thus the policy of the cartel is to interfere in the first instance with the independence of the affiliated undertakings to such an extent that the former character of the undertakings is completely changed. The organisation of the cartel takes over the whole selling activity for the affiliated undertakings and controls the extent of production. The autonomy of the individual undertakings is thus lost to some extent. Still more significant is the economic policy of the highly developed cartels in their relations with customers.

Since the greater part of the total supply of a certain commodity is concentrated in the hands of the cartel, it assumes, a position towards the

individual customers which is the stronger, the more scattered is the demand. Thus it obtains the power to fix prices one-sidedly. The customers have simply to submit to the price policy of the cartels.

However, this by no means exhausts the economic power of the cartels. Cartels of producers aim at bringing the middleman into a dependant position and at eliminating him wherever possible. In many cases an attempt is made to bring the whole process of distribution within the sphere of the cartel. Not only is the technique of production as represented by the undertakings brought under the control of the cartel, but also the whole process of distribution down to the direct consumer. In the endeavour to carry out these aims obstacles naturally present themselves.

Especially do the cartels find it very difficult to induce all undertakings in question to become affiliated. Frequently outside undertakings enjoy all the advantages accruing from the cartel without being compelled to submit to the restrictions entailed by membership. Thus the so-called outsiders become a great danger to the policy of the cartel. It therefore becomes incumbent upon the cartel to induce the outside undertakings to enter into affiliation. This often takes place by the adoption of questionable practices. Violent competition may arise between the cartel and outsiders, which is fought out principally through the regulation of prices.

The outsiders, however, are not the sole opponents of the cartels. Competition with the cartels also develops from another side. Where the cartel embraces the whole of a national economic area, foreign competition may enter into consideration. Where the cartel is only national, in the event of its success, new competition may arise within the national economic area itself. The policy of the cartel must be to fight against or in some way to prevent this opposition.

Cartels make a distinction between those market areas in which they are the undisputed masters of the supply and those in which their mastery is disputed. Within the former they can impose their one-sided prices, whilst in the disputed areas they must have regard to competitors. The possible losses from the sale of goods in disputed areas are made good as far as possible by the charging of higher prices in the undisputed areas.

Dangers to Cartels. The constitution of a cartel is not of a firm and enduring character, and it is threatened by the following dangers.

1. *The failure of its members to keep their arrangements.* Every member is of course obliged to fulfil the terms of agreement and to submit to the terms and conditions of the cartel. As security against unfaithfulness, the cartel has often nothing more than credit documents, such as bills of exchange, which are not always acknowledged by the Courts. The cartel is practically powerless against the secret and indirect transgression of the conditions of the cartel, which is often resorted to by the delinquent members, even if agreements and terms have been most carefully and strictly drawn up so as to safeguard

against such eventualities. Very often it happens that the chief cause of the dissolution of a cartel is the infidelity of its members.

2. *The period of duration.* A cartel is always arranged for a certain period, such as a month or several months, but only rarely for a number of years. The question of the renewal of such an agreement is always a very uncertain matter. Especially during the last period do the members entertain the fear that the cartel will not be renewed, and in such a case they must prepare themselves at the beginning for such times when the cartel will be dissolved.

3. *Outsiders.* The greater the participation of all enterprises of a certain kind in the cartel, the easier can it achieve its purpose of abolishing competition and of maintaining a certain level of prices. The larger the percentage of those who do not join the cartel (i. e., outsiders), the weaker is the cartel. For a cartel to be permanently successful, it is necessary that as many interested firms as possible should join it. However this is a difficult matter.

4. *New promotions.* It is only in the rarest cases that the power of the cartel becomes so great that the promotion or foundation of a new enterprise can be prevented. New firms are constantly arising which compete with the cartel, especially during the period of rising prices. These new undertakings always form a source of annoyance and increasing danger to the cartel.

5. *Dissatisfied Members.* It is clear that the individual members of the cartel consider themselves more or less hindered in their development, the greater the number of functions which are taken over by the cartel. Especially is this the case if the cartel agreement arranges the quantity of output, for then the most efficient firms which would otherwise extend their works are now prevented from so doing. Naturally such firms demand better terms for themselves, which can only be made at the expense of the other members, and therefore a keen struggle ensues. If such terms are refused, these more enterprising units of the cartel may join the "outsiders" and form with them a competing cartel, or, in the last resort, they may be the means of compelling the cartel to dissolve.

The above five points would demonstrate that a cartel can be conducted only with difficulty, and that it is continually liable to dissolution. It is chiefly for this reason that so few cartels have a lengthy term of life, the constitution always being in a state of flux.

The rapid strides made by Germany in industrial development before 1914, especially in relation to overseas trade has been attributed to the highly organised trading methods employed. Of these the most outstanding was the central type of organised selling within the separate industries. The policy behind the German cartels was to consolidate industries by the regulation of production, prices and markets, and thus eliminate baneful competition, and, by more effectively organised national effort, secure an adequate and growing share of international trade.

Such cartels, operating through a selling office or syndicate, fixed quotas of production, or percentage share of trade in allocated markets, or combined these methods. In many cases the German cartels subsidised the export trade out of the additional profits made by increasing the prices charged to home purchasers. As a result of this device German goods could be dumped in overseas markets at prices so low that it was impossible for British manufacturers to compete with them. There was considerable agitation in Germany against this practice; and under the cartel law of 1933 the German Government could compel either the abolition or the formation of cartels as the needs of public policy might dictate.

Japan also used the cartel system extensively in building up her industrial position. The Major Industry Control Law introduced in 1931 regulated industrial cartels and combines. Norway is another country where cartels are governed by law.

The Trust or Combine

Originally the term 'trust' meant a form of business organisation established through temporary consolidation in which the shareholders of constituent organisations under a trust agreement transferred a controlling amount of their shares to a board of trustees in exchange of trust certificates. These certificates showed their equitable interest in the income of the combination. However, towards the beginning of the present century the trusts in America, where they mostly existed, were declared illegal and were dissolved.

At present the term 'trust' is used synonymously with the term 'combine' which signifies a consolidation of capital which is large and strong enough to control the supply and the selling price of the article with which it deals.

The constituent members of a combine fuse together their internal management as well as their external affairs relating to market problems in favour of a new unit. The central organisation decides to a large extent the programme of work and the sales of each participating undertaking. Finance is uniformly regulated for all members, surplus and deficiencies being adjusted within the combine. The distribution of profits takes place on a common basis. All this indicates the close nature of the combination from the point of view of the capital involved.

Trusts or combines grow out of the weaknesses of other looser forms of combination, viz., instability and imperfect centralisation of direction as in a cartel. But they may also grow spontaneously out of the soil of the large industrial enterprises. The spirit of enterprise and the power of expansion which grow with economic success lead to the conversion of the smaller enterprise into a large one, and finally to the establishment of a business on a gigantic scale. It would be a mistake to say that the promoters and administrators of trusts have no other idea than that of making money in their transactions. It is the spirit of enterprise by itself, the entrepreneur's enjoyment of the success of his own work, the intellectual pleasure of thinking out continually new ideas and of realising them, and of assisting in the triumph of mankind over nature by new

achievements that contribute to the growth of such large concerns. Last, but not least, however, must be remembered the pleasure and pride derived by the employer in the development of his personal power and reputation, for this is surely one of the reasons which push most of the promoters of trusts to their goal.

Combines may be of three kinds - horizontal, vertical and circular.

(a) **Horizontal Combine.** This is an amalgamation of manufacturers in the same trade, the purpose of which is to eliminate waste and to develop greater economic power through large scale production, systematic works specialisation, improved methods of distribution, and concentrated research. In addition to these advantages, it may, through its increased capital and purchasing power, obtain raw materials more cheaply, and through its influence enter into agreements with other large combines, and so still further consolidate its position. If the combine is so complete that it constitutes a virtual monopoly it may concert measures to restrict output and fix prices.

(b) **Vertical Combine.** A vertical combine consists of the combination into one organisation of different undertakings, carrying out successive stages in production, from the raw material to the finished article, or even to the retail sale to the consumer. For example, a single aluminium combine may control a company for producing and shipping the bauxite (the raw material); a company carrying on the manufacture of alumina (the pure oxide of aluminium); a hydro-electric company for supplying power; an aluminium smelting company to operate electric furnaces for extracting the metal from its oxide; an aluminium rolling mills and foundry company, a company carrying on the manufacture of aluminium utensils; and a company for carrying on the sale of aluminium domestic utensils to distributors or to the public.

Vertical combines are not so likely to increase as the combines of the horizontal type. Vertical combines aim at securing a position of self-sufficiency. They are combinations of firms engaged in different trades or stages of production of the finished article. By combining these separate interests into one whole, no stage of production is dependent upon outside concerns for the supply of raw materials or semi-finished goods; the combine is one large self-contained and self-supporting unit. But, while this unification may be of considerable importance during a period of violent fluctuations in supply and prices, it is likely to prove disadvantageous in normal times because it ties the combine to its constituent manufacturers, who may not be so favourably placed for business as other manufacturers, outside the combine.

(c) **Circular Combine.** Where several companies engaged in different trades and industries are merged into one large concern, it is a circular combine. The object of such a combination may be partly to effect economy in overhead expenses and partly to insure against the failure in demand in any particular trade. To be able to switch rapidly from swords to plough shares and back again is a happy fate. Indeed, in some cases this mutual insurance of markets is a dominant motive for circular combination.

Methods of creating a Combine A trust or combine may be established in three ways, namely, by amalgamation, by the formation of a holding company or by means of group management.

1. Amalgamation. A more complete form of trust or combine is that of the amalgamation or absorption in which two or more businesses are lined together in a single undertaking, the individual companies losing their separate entities. If a new company is formed to acquire the existing companies, it is known as amalgamation, but if one existing company swallows up a number of existing companies, it is then called an absorption. In America, amalgamation and absorption are respectively termed consolidation and merger. When this kind of combination takes place, one giant undertaking comes into being in the place of several separate business units.

2. Holding Company. In this form each of a group of companies, while continuing to trade in its own name, sells the majority of its shares to a parent or 'holding' company which thereby obtains control of the policy and products of the constituent members. It necessarily involves the formation or the prior existence of another company which has power in its memorandum of association to hold the shares of other companies. The holding company acquires such shares by exchanging its own securities for them or by other means of purchase.

The controlled or subsidiary companies remain nominally independent and operate under their own names, but they are effectively managed by the officers of the holding or parent company, because the latter has the controlling voting power.

3. Group Management. This form of a combine is more elastic and may be described as management by the same persons of a number of companies either engaged in the same trade or carrying on different trades. The companies remain completely separate, but a small group retains effective control of all of them, and works them in harmony. Owing to the widely prevailing system of managing agency in India, this form of combine is very common here. A big firm of managing agents commonly controls a number of companies, which without an actual combination secure all the advantages of buying, selling, marketing, propaganda, research and finance. This subject has been discussed in detail in a previous chapter.

Holding and Subsidiary Companies

As the advantages of a private limited company became more and more known to the public, the number of private companies have increased rapidly since 1913. Many of the private partnership businesses converted themselves into private limited companies, and this process is still going on. A very important result of the legal recognition of a private company and its freedom from publicity was, however, the advent of the holding company, an interesting feature of the joint stock system. The holding company movement started only after 1913

when the private company was legally recognised. From that time till 1936, when the Indian Companies Act of 1913 was completely overhauled, no attempt was made to regulate holding companies by law. Prior to 1936 when the holding and subsidiary companies were brought under legislative control, the term holding company generally stood for any company which acquired control over one or more other companies, so as to effect their policy and management to a large extent either by acquiring a number of shares or in any other way.

The separate recognition of the private company made it very much easier to form large business units consisting of a number of distinct undertakings, each of which was given the legal form of an independent company. Thus a big productive business, instead of starting new works or establishing agencies in new markets directly under its own auspices, could create for this purpose a number of separate private companies, in each of which the parent company held either the whole of the shares, or at least a dominating interest. As these subsidiary companies were generally private companies, there was no obligation upon the holding company to disclose any material particulars with regard to its subsidiary undertakings. The published accounts of holding companies often failed to give any true picture of the position of the subsidiaries, and investors who bought shares in the parent concern had no means of discovering whether the particulars disclosed in the company's published accounts accurately reflected the economic position of the complete undertaking or not. In order to remove this evil, the following provisions were inserted in our company law in 1936 :—

Definition. Section 2 (2) provides that where a company *holds* shares in another company directly or through a nominee *and*

- (a) The amount of shares held is more than 50 per cent of the issued share capital of the other company except where the shares are held as security by a company the ordinary business of which is the lending of money, *or*
- (b) the share holding is such as to entitle the company to more than 50 per cent. of the voting power in the other company, *or*
- (c) the company has power directly or indirectly to appoint the majority of the directors of that other company otherwise than by virtue of the provisions of a debenture trust deed,

this latter company is called a subsidiary company, and subsidiary company includes a subsidiary company of its own. The words "and includes a subsidiary company of its own" are very important, since they expressly provide that a subsidiary company will include its own subsidiaries. In the absence of those words it would appear that where the A Company holds a controlling interest in the B Company and the B Company holds a controlling interest in the C Company, the C Company is not a subsidiary of the A Company (even though the A Company *indirectly* has the power to appoint the majority of the directors of the C Company unless the A Company holds some shares in the C Company).

There is, however, no legal definition of a holding company. But the definition of a holding company directly follows from that of a subsidiary company as given above. A holding company is therefore one which has an interest (as defined above) in one or more subsidiary companies. Although any company which holds shares in another company may be called a holding company, yet the term holding company is legally confined to companies which hold shares in subsidiary companies within the meaning of this section.

It is possible that a subsidiary company may at one time be the subsidiary of more than one holding company. Thus, if A Company has a share capital consisting of 1,200 preference shares of Rs. 100 each (carrying one vote per share) 10,000 ordinary shares of Rs. 10 each (carrying one vote per share), and 10,000 deferred shares of Rs. 1 each (carrying one vote per share and the right to appoint 60 per cent. of the directors), and each class of shares is held by a different company, then the A Company is a subsidiary company of three holding companies, because one holding company holds more than 50 per cent. of the issued share capital, the second holds more than 50 per cent. of the voting power, and the third holds the right to appoint the majority of the directors.

Rights Conferred upon Members of Holding Company. Section 132.A confers on the members of a holding company certain rights regarding the affairs of subsidiary companies, and these rights are :—

(a) The last balance sheet, profit and loss account and the auditor's report of each subsidiary company are to be attached to the balance sheet of the holding company. It means that the shareholders of the holding company are to be supplied with the annual accounts of each subsidiary along with the annual accounts of the holding company. This is the only method by which the shareholders of the holding company may be kept informed about the affairs and the financial position of each subsidiary company.

(b) There shall be annexed to the balance sheet of the holding company a statement signed by the same persons as are required by section 133 to sign the balance sheet of the holding company and showing (i) how the profits and losses of a subsidiary company or the aggregate profits and losses (where there are two or more subsidiary companies) have been dealt with in the accounts of the holding company, and (ii) to what extent provision has been made for the losses of any subsidiary company either in the accounts of that company or of the holding company or of both, and to what extent the losses of any subsidiary company have been taken into account by the directors of the holding company in arriving at the profits and losses of the holding company as disclosed in its accounts.

It is not necessary to specify in any such statement the actual amounts of the profits or losses of any single subsidiary company, or the amount of any part thereof that has been dealt with in any particular manner, nor does the section define the manner in which the profits or losses of subsidiary companies

can be treated by the holding company. In any event the statement to be annexed to the balance sheet of the holding company should disclose the method that has been adopted by the holding company with respect to the profits and losses of its subsidiary companies.

If for any reason the directors of the holding company are unable to obtain such information as is necessary for the preparation of the statement, the directors who sign the balance sheet shall so report in writing and their report shall be annexed to the balance sheet in lieu of the statement.

There is a contradiction in this section, for while it provides that the statement need not disclose the actual amount of the profits or losses of any subsidiary company, yet the last audited balance sheet, profit and loss account and the auditors's report of each subsidiary company are to be annexed to the balance sheet of the holding company.

If the auditors' report of any subsidiary company is qualified in any respect, the statement to be annexed to the balance sheet of the holding company, as described above, must contain particulars of the manner in which the auditors' report is qualified. The inclusion of such qualification in the statement is, however, quite unnecessary in view of the fact that the auditors' report itself is to be circulated to the members of the holding company.

(c) A holding company may by a resolution authorise representatives named in the resolution to inspect the books of account of any subsidiary company, and on such resolution being passed those books of account shall be open to the inspection of those representatives at any time during business hours. This is a valuable privilege granted to the shareholders of the holding company.

(d) Under section 138, the shareholders of a company have a statutory right to appoint by special resolution inspectors to conduct an investigation into the affairs of the company, if they have reason to believe that it is being mismanaged. This has a very salutary check upon the management of the company. A similar right has been given to the members of the holding company in respect of each subsidiary company. That is to say, the members of a holding company can appoint, by passing a special resolution, inspectors for investigating the affairs of each subsidiary company.

Withdrawal of Certain Privileges of Private Companies. A private company, on becoming the subsidiary of a public company, ceases to enjoy a number of privileges granted to private companies, so that the shareholders of the holding company, who become directly interested in the affairs of that subsidiary company, may have some protection against abuse on the part of the management. The privileges that are thus taken away from a private company on its becoming the subsidiary of a public company have already been stated in a previous chapter.

Additional Information in Holding Company's Balance Sheet. Under section 132 (2), the balance sheet of a holding company must disclose information relating to secured loans due to subsidiary companies, unsecured

loans due to subsidiary companies, advances to subsidiary companies, and investments in the shares, debentures and bonds of subsidiary companies. These things are to be separately shown on the balance sheet of the holding company; but in each case only the aggregate amount is to be stated. It is not necessary that the figures relating to each subsidiary company should be given separately. Trading debts due by or to subsidiary companies are not, however, to be shown separately on the balance sheet of the holding company.

Directors' Remuneration. Where the directors of a holding company are, by virtue of nomination, also the directors of a subsidiary company, any remuneration received by them from the subsidiary companies must be disclosed by way of a footnote on the profit and loss account of the holding company, so that the shareholders thereof may know how much remuneration the directors are receiving from both the holding company and its subsidiaries.

Advantages of Holding Companies. 1. The principal use of the holding company system is that it enables the benefits arising from the amalgamation of two or more companies to be obtained without the loss of any of the advantages that may attach to the preservation of the names, goodwill, and separate organisations of the constituent businesses. By acquiring the whole or a controlling interest in the share capital of the subsidiary companies, the policy and management of these companies may be just as effectively controlled and directed by the holding company as if all the members of the group were welded together into one legal entity. Thus without a formal amalgamation, it is possible to secure elimination of competition, economy of costs and increased co-ordination and efficiency.

2. Although a holding company possesses a controlling interest in the subsidiary companies and follows a central and coordinated policy of management, yet the several subsidiaries are free to pursue their own business policies as determined by their managements who can best judge local conditions and requirements.

3. The financial needs of the subsidiary companies can be easily met by the holding company whose financial position in the money market is usually strong, whereas each subsidiary company may not be strong enough in that way.

4. The accounts of each unit in the combine are prepared separately and are therefore easier to understand than the combined results of the whole organisation.

5. Even where there is no practical objection to a complete amalgamation, the holding company structure is advantageous in as much as it enables the merger to be carried out without disturbing such parts of the capital of the separate companies as may be represented by preference shares or debentures carrying rates of dividend or interest favourable to the company. In such cases effective control may be obtained by the acquisition by the holding company merely of a majority of the class of shares which carry the voting power.

6. The system possesses an advantage from the taxation point of view,

since by preserving the separate legal entities of the constituent companies, the right to carry forward against future assessments any past losses or unabsorbed depreciation will not be lost, which right would cease if the constituent companies would have gone into liquidation for the purpose of amalgamation.

Evils Associated with Holding Companies. The system of holding and subsidiary companies, if adopted for a *bonafide* purpose, is capable of immense good both to the shareholders of the holding company and the public at large. But in practice the system is not worked with the same idea and integrity which it deserves. It is often employed as a tool for improper purposes. Once the system falls into the hands of unscrupulous people, it is capable of doing great injury to the investors and the public. The following are the principal evils associated with the system of holding companies :—

1. There is a possibility of inter-company manipulations operating to the detriment of the minority interest in the subsidiaries by the invoicing of goods by one company to another at less than current market prices, or by the making of loans by one company to another without adequate interest or security.

2. The tendencies of a holding company may be somewhat anti-social. It may place almost complete power over a number of companies in the hands of a few men, who may with their stronger financial resources crush all independent competition and dictate their own terms to purchasers of their products.

3. The investing public may be exploited through overcapitalisation of holding companies and promoters may secure large profits by the sale of water stocks.

4. The concentration of control in the hands of one board of directors may result in the responsibilities proving more onerous than the executive is capable, by ability and experience, of successfully accomplishing.

5. Large groups and combines tend to become soulless and fettered with undue redtape, thereby destroying individual initiative and enterprise. In the absence of efficient organisation, customers may lose the valuable sense of personal relationship.

Distinction between Cartels and Combines

Cartels are loosely allied combinations which have the organisation of individual units unaffected and confine their activities to marketing either by fixing prices or by fixing the quantities produced by the individual units, or by both. Their aim is, therefore, not so much the lowering of the costs of production as the securing of monopoly profits; they can be directed against the consumer and their formation is not followed by real advantages to the consumer. Combines or trusts, on the other hand, are closely allied combinations which serve to increase the efficiency of production by concentrating production in the most economical units, by scrapping obsolete plant, by introducing scientific management and all the other devices grouped together under rationalisation. Their ultimate effect is, therefore, rise in productivity, rise in wages, rise in general welfare.

iron ore and coal, and therefore purchase their own coal mines, coke ovens and iron mines; further the combine may build its own ships in order to become independent in regard to the transport of raw materials and of the finished products. The kernel of the combine is its capital, the extent of which enables it to promote, acquire, combine or conduct any kind of undertaking. Since the capital is organised by banks and other financial institutions, these are generally closely connected with the combine, and are thus able to control the promotion of new businesses, the granting of credit, and can assist the combine in developing new lines which are considered to be profitable.

Advantages of Combination. Great possibilities of industrial and commercial improvement lie beyond the confines of free competition, and are to be realised by combination in one or other of its several forms—by informal consultation and co-operation, by formal association or by actual amalgamation. The advantages of combination may be stated to be as follows :—

1. *Economic in Production.* Purchases of raw materials, stores and spare parts of machinery can be made in bulk with the advantages of better selection, better terms and lower transport charges; middlemen can be eliminated and the control over the sources of material can be acquired. As regards manufacture, it is possible to arrange for a standardisation of parts and sizes throughout the industry whereby production can be greatly cheapened and the parts of one maker made interchangeable with those of another.

Again it is possible to arrange that instead of every firm trying to cover the whole ground, each shall devote itself to some particular section and instal specialised equipment for its own section and for that only, in which case wasteful duplication can be avoided and specialised skill developed. Further, whereas under free competition the firms in one district may be working overtime while those in another district are on short time, it is possible with combination to maintain something like an equal distribution of work and to control orders so that the volume of work does not fluctuate so greatly from one period to another.

Factories, which are most favourably situated for economical operation, can be utilised to their full capacity, and those unfavourably situated can be closed down. More expensive but efficient plant can be purchased.

2. *Economy in Finance.* The aggregate working capital of a number of separate businesses is normally greater than what would be required by a combination of such businesses e. g., a combine can transfer the stock-in-trade from one branch to another to make up a temporary shortage. Finance can be raised on better terms, and the temporary investment of surplus funds can be made more advantageously.

3. *Economy in Administration.* The total number of directors, managers and the general staff may generally be reduced below the aggregate numbers previously employed in the separate businesses, and the administration

and control of the combined business may be entrusted to the ablest of those formerly engaged in the separate businesses, who may be enabled each to specialise to a greater extent than was formerly possible. The greater opportunities of promotion available in a combine attract and retain the most competent men.

4 *Economy in Distribution.* The cost of advertising is reduced or the same expenditure may be made more effective. Even, where the identities of several businesses are retained to have separate goodwill, collective advertising may be resorted to for the benefit of all. Advertising can be localised according to known demand in various districts and better terms can be obtained for advertising campaigns. Better terms of credit and greater choice of goods may be offered to customers. Competition among the several branches can be avoided. Economy may also be achieved by preventing overlapping in connection with the activities of travellers and salesmen. Each factory or depot can supply its own area, thus effecting saving in transport charges.

Moreover for a country carrying on a large export trade, representation in foreign markets is a matter of primary importance, and it has become increasingly apparent that independent manufacturers, if they combine for nothing else, must combine for the purpose of pushing their goods abroad if they wish to keep and extend their foreign connections.

5 *Maintenance of Selling Prices.* The elimination or reduction of selling competition renders price-cutting unnecessary, and economic prices can be charged for all products. Better control of selling prices and conditions of sale is also secured.

6. *Exchange of Knowledge.* Under competition every one of a host of small manufacturers works out his own problems, evolves his own methods and processes and keeps what he knows to himself. When a combine is formed this secrecy is ended and anything worth imitating at one branch is available for all the others. It is possible for a combination to secure the pooling of resources and brain power and improved facilities for research.

Evils of Combination. Against the advantages of combination must be set some possible evils. These are :—

1. *Monopoly.* The chief evil associated with combination arises from the possible creation of monopoly and the restraint of trade with the public suffering as consequence. The elimination of healthy competition may result in the unfair increase of prices ; or the powerful organisation may attempt to eliminate smaller businesses in the same trade by a 'price war' followed by an exploitation of the monopoly thus created.

2. *Inefficient Management.* A large combination may entirely lose the personal element formerly existing when the business belonged to individual proprietors. Further the combination may result from the efforts of one man, who may be able to control and manage it quite well during his lifetime ; but such giants of commerce and industry are few, and when one passes away there

may be no one big enough to take his place, with the possibility of the break-up of the business.

3. *Lack of Initiative.* Through the heads of an independent business may be willing to spend toilsome days and anxious nights in developing an idea which holds out some promise of greatly raising its status, yet the same man may be rather supine in such matters if they know that the honour and reward which may result from their exertions will belong to the combination, and thus the spread of combination may dry up the sources of truly original invention.

4. *Overcapitalisation.* It is maintained with a great deal of truth that combines are generally overcapitalised and suffer from the evils attaching to overcapitalisation and also from gambling speculation by the directors. Investors and shareholders are often and often grievously wronged.

5. *Injury to Labour.* A combine can control labour and volume of employment. Economy of large scale production is not generally transferred to labourers in the form of higher wages, as there is nothing to compel the combine to do so. It can also reduce employment by underproduction.

6. *Corruption.* A grave evil associated with large combines is that they with their vast resources are able to buy and do often buy legislators to do their bidding and in this way they corrupt the political life of the country. The interests of the public are sacrificed to promote the corrupt and selfish interests of the combines.

7. *Unequal Distribution of Income.* The existence of great concentrations of economic power makes nonsense of democracy. The control of employment, the control of what is to be produced, and through the control of prices, the distribution of income between the various classes of society are in the hands of small and solid groups responsible to no one and subject to no control.

Big Business. The term "Big Business" came into use in America at the beginning of the 20th century. It stands for the concentration of capital resources and control of allied businesses into the hands of a few persons.

The factors favouring the growth of big business have already been examined in the preceding pages. To put it briefly, business tend to become big in order to eliminate competition, to secure economies of large-scale production, and to acquire a sense of aggrandisement. A business may become big in three ways—

(1) It is born great when it is big from its very inception, such as the United Commercial Bank Ltd.; the Hindustan Motors, Ltd.; and a number of other gigantic concerns brought into being during the last few years.

(2) A business achieves greatness when it slowly grows into a big unit under capable management, e. g., the Tata Iron & Steel Co., Ltd.; The Titaghur Paper Mills, Co., Ltd.; The Oriental Government Security Life Assurance Co., Ltd.; the Central Bank of India, Ltd.; etc.

(3) A business has greatness thrust upon it when it is a combination of

several units, such as the British India Corporation, Ltd., Associated Cement Companies, Ltd., etc.

Combinations in India

Compared with Western countries, the combination movement has been very slow in India. There are several reasons for this. Firstly, we are industrially backward, so there has been no great need for combination. Barring solitary exceptions, industries in India have not reached a stage when combinations are necessary and can be made effective. Secondly, our industrial leaders have adopted an individualistic attitude as regards combination, they like to plough their lonely furrows. And finally the managing agency system, which in many cases provides the economies of combination by means of group management of industrial units, has been responsible for the absence of formal combinations.

A brief review of the combinations formed in India is made below.

Managing Agency System. In India, there has been no evolution for combinations in industry, as had been the case in the West, but there have been combines in this line or that according to exigencies of circumstances. The most familiar type is the financial integration as a result of the existence of the managing agency system. Owing to the ramifications of this system the chief characteristic of our industrial development has been the concentration of control and management of a large number of companies into the hands of a small group.

This financial integration by the managing agency system has been in the same line (as in the case of cotton mills of Bombay and Ahmedabad) as well as in different lines. The latter, however, resembles neither the vertical nor the horizontal type.

The financial integration has assumed diverse forms inter-company investment being prominent. Very often surplus funds of a concern are deposited with the managing agency firm, which in turn uses the same either in its own business or in another concern under the same managing agency. Funds are sometimes raised on the credit of one concern but used for another.

However such an integration is criticised from the point of view of sound company finance, the fact remains that when sufficient funds were not coming forth from the investing public and when there has been dearth of institutions for supplying long-term finance in the country, this sort of integration was imperative. Indirectly, it has led to a greater degree of cooperation among the different units, financially tied with each other.

Amalgamation or merger. Cases of amalgamation or merger have been scanty, and most of them were under the pressure from the managing agency firm, managing the combining units. Another aspect of the feature is that such amalgamations have not clearly taken the form of either horizontal or vertical. Rather concerns following different lines have been merged, because the same managing agent may have interest therein. The British India Corporation, Ltd., is a glaring example.

The B. I. C. was formed in 1920 to take over six separate companies engaged in different industries, namely, The Cawnpore Woollen Mills, Ltd.; The Cawnpore Cotton Mills, Ltd.; The New Egerton Woollen Mills, Ltd.; The North-West Tannery Co., Ltd.; Cooper Allen & Co., Ltd., and the Empire Engineering Co., Ltd.; This Corporation also controls four subsidiary companies.

The biggest merger hitherto formed in this country is the Associated Cement Companies, Ltd. It came into existence in 1937 in order to amalgamate eleven cement manufacturing concerns. The Cement Agencies, Ltd., act as the managing agents of this huge combine. In addition to taking over the factories of the constituent companies, the A. C. C. has erected a factory at Rohri in Sind and another near Bezwada.

Besides the above two big mergers, there have been others, a few of them being (a) Burrakur Coal Co., Ltd., acquired in 1919 eight coal extracting companies, seven by merger and one by purchase, (b) Madura Mills Co. Ltd., absorbed the Coral Mills in 1924, the Tinnevely Mills in 1927, and the Pandyan Mills in 1929, (c) The Buckingham and Carnatic Company, Ltd., Madras, is the outcome of amalgamation of three cotton mills under the same managing agency firm; (d) The Bangalore Woollen, Cotton & Silk Mills Co.; Ltd., acquired the Kaiser-i-Hind Woollen, Cotton & Silk Mills Co. Ltd., by purchase.

Pools and Cartels. There are isolated examples of pools and cartels formed in India, but most of these have been very ineffective.

1. The Indian Sugar Syndicate Limited at Kanpur is the most well-known organisation, which is truly speaking a cartel controlling the supply and distribution of sugar for all sugar factories in the United Provinces and Bihar. It was formed in 1937, but its work was suspended in 1943, when sugar was controlled by the Central Government. It has again resumed work since November 1947, when sugar was decontrolled. The Syndicate has been successful in steadying the sugar prices and planning and undertaking equitable distribution of sugar in the country.

2. The Cement Marketing Company of India was established in 1930, with the efforts of the Cement Manufacturers' Association, the object being to take over the control of sales and distribution for almost all the manufacturing companies in its membership. But the Company could not achieve great success, and hence the necessity of complete fusion was felt, which materialised in 1936 by the formation of the Associated Cement Companies.

3. The Indian Jute Mills Association which started its career in 1886 presents before us a sound example of a so-called simple association, which has been successful in achieving the aims of an 'output pool'. This association represents 95 p. c. of the trade, and in 1910 its membership stood at 73, including all but 11 of the smaller mills of India which collectively represented only 5 p. c. of the total loom strength. The member-mills have, from time to

time entered into agreement for restriction on hours of work, for adjusting supply to market demand and closing down a certain percentage of the loom.

Shipping Rings. There is also a division of the market among the units and meeting may be made of shipping rings and conferences. There has been an agreement between the British India Steam Navigation Company Ltd. and the Scindia Steam Navigation Company, Ltd. In inland navigation also we find the existence of freight agreements such as the one existing between the India General Navigation and Railway Co. Ltd., The Bengal Assam Steam Shipping Co., Ltd., the River Steam Navigation Co., Ltd., and East Bengal River Steam Shipping Co., Ltd. regarding the carriage of jute from the inland centre to terminal markets. These shipping companies enjoy the exclusive right of carrying jute waterways for the members of the Indian Jute Mills Association and the Calcutta Baled Jute Association under agreements. They are, therefore, known as the 'Agreement' or 'Conference' companies.

Agreements. Voluntary agreements have sometimes been entered into at several occasions to meet certain contingencies, but as is generally the case with such agreements elsewhere as well, such agreements remain a failure, and hence are easily terminated. The paper industry in India presents an example of a permanent and strong agreement, although voluntary in nature. The policy of the mills belonging to the Indian Paper Makers' Association and also of those working conjunction with it has been to combine by agreement for the purpose of price fixation and for the allotment of the contracts with the Central and Provincial Governments which represent 20 to 25 p. c. of their production, according to an agreed arrangement among themselves. The agreements have been successful because until very recently there was a practical monopoly of trade between the three older mills, viz., the Titaghar Paper Mills Co., the India Paper Pulp Co. and the Bengal Paper Mills Co. The new mills that have of late come into existence have either joined or are cooperating with the Association. The combination has enabled the mills to maintain prices at a level slightly below the level of prices quoted for imported paper of similar quality.

Holding Companies. As a matter of fact, many companies in India hold shares in other concerns and specially so when they are under the same managing agent. But holding of shares in other concerns for acquiring effective control is not so common with the industrial concerns. Investment trusts, formed exclusively for the purpose of investing money in different industrial concerns for investment as well as for acquiring control, have been formed to a certain extent in India, but their control has not been so effective on account of the existence of more powerful managing agents, who have de facto a complete control over most of the industrial concerns, specially in the cotton, jute and engineering industries.

Test Questions

1. Account for the recent tendency towards the formation of business combinations.

(Rajputana B. Com. 1949).

2. Examine the effects of an increase in the size of an industrial undertaking on the relations between labour and management.

(Bombay B. Com. 1943).

3. "Combinations by giving rise to monopoly harm the interests of consumers." "Combinations by reducing costs offer goods and services at lower prices to consumers." Reconcile these views.

(Bombay B. Com. 1943).

4. Indicate the chief reasons for the modern tendency towards amalgamation of business undertakings. Point out the effects of such amalgamations.

(Bombay B. Com. 1942).

5. Describe the various forms which agreements to limit competition among producers and sellers may take.

(Bombay B. Com. 1934).

6. How do you explain the slow appearance of combination in Indian industry?

(Bombay B. Com. 1935).

7. Distinguish clearly between a "Vertical" Combination and a "Horizontal" Combination. What are the motives which lead to the formation of such combinations?

(Bombay B. Com. 1938).

8. What are cartels? Discuss the causes that favour the growth of cartels, and the difficulties in their successful operation.

(Allahabad B. Com 1937).

9. Give the main classification of business combinations. Illustrate your answer from Indian conditions.

(Agra B. Com. 1948).

10. What are the chief causes that lead to combination in industry and trade? Illustrate your answer from Indian conditions.

(Agra B. Com. 1947).

11. What is a holding company? How does it differ from a trust or pool? What are the objects of such combinations?

(Agra B. Com. 1942).

12. Point out the relative merits and defects of holding companies, trusts and mergers as forms of combination in business.

(Bombay B. Com. 1946).

13. Discuss the important features of a cartel. Are there any cartels in India? If so, name them. Do you believe that the introduction of cartels can benefit Indian Industries?

(Agra B. Com. 1946).

14. What is 'Big Business', and why do business tend to become big? It is said that 'some businesses are born great, some achieve greatness, and some have greatness thrust upon them'. Discuss this statement with Indian examples.

(Agra B. Com. 1945).

CHAPTER 8

FINANCING OF BUSINESS CONCERNS

Every business requires capital in greater or smaller quantity, and the purpose of this chapter is to discuss the methods of finding the capital necessary for starting a new business or for developing an established one. The subject of financing business concerns falls into two parts, namely, finding capital for proprietary concerns and finding capital for public limited companies.

The proprietary concerns consist of one-man businesses, partnerships and private limited companies, in which both the control of the capital and the management of the business are usually in the hands of the proprietors themselves who are only a few in number. There cannot, for instance, be more than twenty partners in a firm, nor more than fifty shareholders in a private limited company. In a public company, on the other hand, the number of members may be very large, and, owing to the ease with which their shares can be sold through the medium of stock exchanges, the composition of shareholders is constantly changing. Therefore the management of the affairs of a public limited company cannot be vested in the proprietors, the ownership of a capital is divorced from the management of the undertaking, and control is delegated by the shareholders to a board of directors, who are responsible for the general direction of the business. Though it is the business of directors to determine matters of general policy, the actual management of the company's business is usually entrusted to managing agents.

It must not be supposed, however, that the divorce of capital ownership from management in the case of a public limited company is necessarily an evil. The directors and the managing agents, who constitute the management of the company, know much more than the shareholders about the business of the company, and a conscientious management has the interests of the company at heart. It usually takes the long view, while the shareholders take the short view. Frankly speaking the shareholders of a company want to get out of it as much as possible, as they are here today but may be gone tomorrow. Hence the interests of the management and those of the proprietors come into conflict. Many a good management, towards the end of the company's financial year, spend a lot of time in devising means of concealing profits from its shareholders so that the company may have hidden reserves to fall back upon in times of adversity.

Most of the proprietary concerns are of the smaller type, while the businesses owned by public companies are of the larger type. The usual evolution is from the one-man business to the partnership, from the partnership to a

private limited company, and from the private company to a public company. A business may be started through the efforts of an enterprising individual. When it has proved a success, additional capital is secured from others who are taken into partnership, and a private limited company may then be formed to limit their liability. As the business grows further and its success is established, the public may be invited, by converting the private company into a public company, to furnish the additional capital needed.

The various methods by which the necessary capital is secured for a proprietary concern and for a public company will now be examined in detail.

1. Financing of Proprietary Concerns

It is stated above that the proprietary concerns are usually smaller businesses; but that is not always the case. There are a number of large-sized undertakings that fall in this category, but they are almost always family concerns that have grown during several generations, and this is particularly the case in this country where the joint family system has been in existence for centuries.

When it is proposed to start a new business, the promoter must have a very clear idea of the nature of the business and the finance required for its successful conduct. It is, of course, true that no new business is ever called into existence all at once; it usually passes through a process of gradual expansion. Before the promoter undertakes the venture, he must examine the whole question carefully in order to consider the volume of business he is likely to transact. All this applies whatever the nature of the business may be. In a purely trading concern the promoter must estimate the minimum and maximum turnover; while in the case of a manufacturing business he must consider the volume of output that he is likely to dispose of and the means by which he proposes to create it. If a new business is started haphazard without any well-considered estimate of the finance required, it is just possible that the lack of capital may be a serious handicap and it may damage the reputation of the business at the very outset instead of building up a valuable goodwill.

In all cases it is not always necessary that the whole capital required should be raised at the outset. If the promoter can arrange to raise the necessary capital by instalments as required, it will be a comparatively economical method; but it is important to have everything settled on a satisfactory and business-like basis, so that the proprietor or proprietors concerned may know exactly where to find the money from time to time for the purpose of the business.

The finance required for carrying on a proprietary concern may be obtained from five principal sources:—(a) The private resources of the proprietors; (b) Loans from friends and relatives; (c) By taking a partner; (d) Loans from banks; and (e) Loans from the public usually by means of *hundis*.

(a) *Own Resources.* The principal method of financing a proprietary concern is by means of the resources of the proprietors. So far as the capital which is the property of the proprietors themselves is concerned, that naturally

is a quite satisfactory form of capital, particularly if it does not represent the whole of their private resources but leaves them a certain margin for contingencies, so that they may not require to withdraw part of their capital for living purposes if profits are delayed. It may be easier to find outside capital for an existing business which has proved its worth than for a new one whose success is yet to be seen. If a person tries out a new enterprise with his own capital, he will naturally put forth his best into it and a year or two's experience will bring to light any defects in his original scheme thus showing him the best method of development.

A business should not be allowed to expand too rapidly, or disaster as sudden as the bursting of a toy balloon may ensue. Indeed many business failures have been due to overtrading induced by early prosperity and an optimistic belief that failure is impossible. If the actual trade falls considerably below the expected minimum the results are very unsatisfactory; but at the same time it is desirable to point out that any considerable increase beyond the expected maximum trade may have equally embarrassing results. The latter state of affairs is known as overtrading, i. e., trading beyond one's means.

Overtrading, in other words, means that the trader purchases and sells goods and receives and grants credit to an extent not justified by the amount of his capital. The state of overtrading may be brought about in two ways: A trader may start business with insufficient working capital or his capital may have been reduced by trading losses or personal drawings. Whatever the reasons for the overtrading may be, its consequences to the trader are serious. He cannot pay off his creditors on the due date. This would damage his business reputation and he may not be able to obtain further credit when purchasing goods. He cannot make purchases at the best price obtainable, because he is not in a position to pay ready cash. He cannot carry sufficient stocks and therefore cannot give prompt delivery to his customers and this will adversely affect his sales. He may be obliged to allow large cash discounts to his debtors in order to induce them to pay before the due dates. He may not be able to tide over a period of bad trade and his business may have thus to be closed down.

A healthy business is one that constantly grows, it needs more and more capital continually. As it grows more money has to be put into furniture and fixtures, stock debts and stocks. The soundest method of financing growth is to retain profits in the business, the proprietor drawing out less than the business earns. Part of each year's profit is then set to earn further profit in the next year, and so long as the proprietor can keep this process going, his interest in the business and his wealth increase steadily, and the business too remains in the fullest sense his own property. Many of the well-established proprietary concerns in this country owe their present position to this prudent policy on the part of their proprietors followed over a long period.

(b) **Loans from Friends and Relatives.** Unless the proprietors of a business are very wealthy, a business may stand in need of outside capital. It is, however, desirable that the funds that are more or less permanently invested in a business should remain as capital so long as it is continued. The raising of capital by methods dependent for their permanence on the pleasure of the lender is always unsatisfactory. At any time the business may be called upon to refund these advances; and if this is the case it will in all probability be at a time when it will be most inconvenient to find the money elsewhere. In the case of loans taken from friends and relatives, the arrangement can only be satisfactory if the advance is for a stated term of years sufficiently long to make it worth while to use the capital in the meantime, and to take the trouble of replacing the loan or readjusting the arrangement at a later stage when the first loan matures.

The manner in which capital is provided by the friends and relatives of the proprietor of a business may vary according to circumstances. It usually takes the form of a loan at a fixed rate of interest or carrying a share of the profits earned, repayable at a fixed date or dates or on certain contingencies such as the death of the lender or the marriage of his daughter, and so on. In the case of well-established proprietary firms in the country, the munims and other employees also usually supply a certain amount of capital by way of deposits carrying a specified rate of interest and repayable on demand.

(c) **Taking a Partner.** If additional finance is needed for an ever-expanding proprietary business, a permanent arrangement that may be resorted to is the admission of a partner with money to bring in. If the partner is a man of ability, there will be ample scope for his services in a thriving business. On the admission of a partner it is usual for the original proprietor to put an agreed value on the goodwill he has created. The value is then added to his capital account and is debited to a Goodwill Account which afterwards appears as an asset in the partnership balance sheet. As the goodwill of the business owes its existence to the efforts of the first proprietor, it is only fair that its value should be placed to the credit of his capital account. The new partner's capital then buys part of the goodwill of the business as well as part of each of the other assets.

The proprietor of a business should regard himself very fortunate if he can find a partner in a congenial friend, who is prepared to contribute capital and share equally in the management with him. His responsibility is halved, and the business is not dependent on a single individual. If the proprietor of an established business does not want that anyone else should share with him in its management, it may be possible for him to find a financing partner, i. e., one who is prepared to contribute capital for share of the profits but who is not keen on taking part in the management of the concern.

(d) **Loans from Banks.** When additional finance is needed for an expanding proprietary business, and it is not expedient to raise it from the

friends and relatives of the proprietor, recourse may be had to bank loans. A commercial bank makes temporary advances to augment the working capital of a business, but it does not provide the permanent capital. In granting loans to business concerns, commercial banks take certain steps to ascertain the standing and repute of applicants for loans. Banks have their own intelligence departments which, by watching markets and the operations of dealers in those markets, by the receipt of information from many sources open to them, confidential and other wise, by the examination of books and balance sheets and the summing up of the information so received by the officers of the bank, arrive at their estimate of the credit that should legitimately be granted.

Banks in India usually insist on a full backing of tangible and easily realisable security for their loans and take no account of the personal credit and integrity of the borrowers. This is in striking contrast to the position in England where bank loans granted to business concerns are to a certain extent without any tangible security. Moreover, banks in this country insist on maintaining a margin of some 20 per cent in regard to advances against stocks. Banks finance business concerns out of their short-term deposits by granting advances for working capital for short periods. Though they are always willing to renew these loans from time to time provided that the borrower's business is running satisfactorily and the security is good, from the point of view of the borrower this position is considered to be precarious in view of the fact that the concern can never be certain of getting a renewal of the advance.

The rates of interest charged by banks for loans and advances to business concerns is fairly high. For example, the usual rate of interest for bank loans and advances is generally the Imperial Bank of India's rate, and in some cases one or two per cent higher. As the Imperial Bank of India rate increases with reference to seasonal market conditions, business men are penalised by high interest charges based on seasonal stringency of the money market. Again, before trader can secure a bank loan, he has to comply some irksome formalities. We, as a nation, hate formalities and like simplicity.

Owing to the fact that banking facilities are not available in all places in India and also owing to the formalities discussed above observed by banks in granting loans and advances to business people, this method of financing proprietary business concerns is not very common. Of course, with the recent increase in the number of banks and their branches, business men have begun to take an increasing advantage of banking loans and advances, but it will take a long time before people make the fullest possible use of banking facilities.

(e) **Hundis** By far the best and most popular method of raising finance for proprietary businesses in this country is by means of hundis. Hundis are the oldest instruments used in business for securing temporary funds from the public and especially from indigenous bankers. The word "Hundi" according to some writers is of Persian origin and its literal meaning is said to be "to collect". Other writers, however, state that the word Hundi is a corruption

from the word Hindi or Hindu. Very likely the latter derivation is more accurate in view of the fact that the hundi is the oldest instrument surviving from ancient times, as there is a legendary story, that Vastupal Tejpal drew a hundi of ten crores on the Nagar Seth ("City Banker") of Ahmedabad and that the temples of Dilwara on Mount Abu were built with the money. Another legend of the times of Lord Krishna has it that Narsinha Mehta of Junagarh drew a hundi on Seth Samalsah of Dwarka about 2,500 years ago.

Although a hundi has existed from very early times, there is no legal definition of the term available. Section 5 of the Indian Negotiable Instruments Act of 1881 contains the definition of a bill of exchange which is applicable to bills, promissory notes and cheques. The hundis, as a rule, are deemed to lie outside the provisions of the Act. A hundi is governed by the time-honoured customs and usages of the various localities. It is only where no specific customs obtain that a hundi is treated as a bill of exchange within the meaning of the Act. In simple words, a hundi may be defined as a written order, usually unconditional, made by one person on another for the payment, on demand or after a specified time, of a certain sum of money to a person named therein.

Again, it must be pointed out that a hundi is not quite an inland bill of exchange which it is commonly made out to be. The main function of the hundi is to enable a merchant to obtain finance. A merchant who needs money may draw a hundi on his agent or himself ordering to pay a specified sum of money to the person named therein after a stated period of time. The person to whom the hundi is made payable is the lender who advances the amount mentioned in the hundi and the usance of the hundi is the period for which the advance is made. Such a hundi is known as *mulatti* or *milli* hundi. Let us take an illustration. Suppose a proprietary concern of Agra (known as Atma Ram & Sons, kirana merchants, its present proprietor being Lala Ram Gopal) is in need of a sum of Rs. 10,000 for purchasing a large stock of dried fruits for the ensuing winter season. The proprietor cannot put in this money from his private resources nor does he want to go to a commercial bank for an advance, but he wants to raise this finance by issuing a hundi for a period of four months when the new stock will be sold and he will be in a position to repay the loan. Lala Ram Gopal then calls a hundi dalal and gives him the necessary instructions. The dalal then goes round to the various persons and firms who have spare money to invest for a short period; and it is found that one Pandit Govind Prasad, a wealthy zamindar, is willing to lend Rs. 10,000 to Atma Ram & Sons for four months, because he has spare funds to invest and he knows that the credit enjoyed by the borrowing firm in the bazar is good. He therefore hands over Rs. 10,000 to Atma Ram & Sons through the dalal. Atma Ram & Sons then draw a hundi in the following form and gives it to the lender :—

सिद्ध श्री आगरा शुभम्याम श्री पत्री भर्दि आत्माराम एष्ट सन्स जोग निव्री

आगरा से आत्माराम एण्ड सन्स की राम राम बचनना आगे हुन्डी किता १ तुम्हारे ऊपर करी रुपइया १०,०००) अंकेन रुपइया दस हजार के नीमे रुपइया पाँच हजार के देने देना। यहाँ राखे भाई पंडित गोविंदप्रसाद के मित्ती मंगसिर वदी ११ से दिन १२१ पाछे सहा जोग चलन बाजार बिना जापते ठिकाना लगाय चौकस कर दाम देना।

हुन्डी लिखी मित्ती मंगसिर वदी ११ सम्बत् २०८५।

In this specimen of a *mitti bundi*, Atma Ram & Sons are the drawers (*Likhnevala*). They themselves are also the drawers and Govind Prasad is the payee (*Bakhnevala*). It is signed by Ram Gopal, the proprietor of the borrowing firm. It requires a stamp of Rs. 1.4 0, as the stamp duty on hundis drawn in the United Provinces is at the rate of two annas per Rs. 1,000. Formerly the stamp duty on hundis was fairly high; but when the Congress Government came into power it reduced the stamp duty on hundis to two annas per Rs. 1,000 in order to make their use more popular amongst Indian business men. The amount and the usance of a hundi depend upon the amount of the loan and the period for which it is taken.

The period stated in a hundi is expressed according to the Samvat era and is always stated in odd days, such as 31, 61, 91, 121, 151 days, because we believe the odd numbers to be auspicious.

The interest on an ordinary loan is payable either half-yearly or yearly or along with the repayment of the loan itself. But in the case of hundis, the interest (called *Hundiyan* or *Hundiyanan*) is paid by the borrower to the lender at the time of taking the loan. The rate of hundiyan depends upon the credit of the borrower, the state of the money market and the period of the hundi. It is quoted at so much per cent. for the whole period of the hundi. If in the above example the rate of hundiyan is Rs. 1.6.0 per cent., Atma Ram & Sons will have to pay back to Govind Prasad a sum of Rs. 137.8.0. Each party will have to pay a small sum to the *dalal* for his services.

A hundi may be endorsed like a bill of exchange. The endorsement on a hundi is known as "*Bechi karna*". A hundi may be endorsed in two circumstances, i. e., (i) when the holder thereof stands in need of money and (ii) when the credit of the borrower is not good and he is required to produce a surety before his hundi is taken up by an intending lender. In the example above cited, if Govind Prasad stands in need of money say two months after the date of the hundi he may sell it to someone else by paying him hundiyan for the remaining usance of the hundi. Or, if the *bazar* credit of Atma Ram & Sons is not good, Govind Prasad may not be willing to lend Rs. 10,000 to them unless they find a surety who will endorse the hundi in favour of Govind Prasad. The procedure then will be as follows. Suppose Atma Ram & Sons find one Bulaki Dass, who is prepared to act as a surety for them. Then the hundi is in the first instance drawn in favour of Bulaki Das who will then endorse it in favour of Govind Prasad. Bulaki Das will, of course, charge a small commission for this service.

The due date of a hundi is calculated according to the period stated therein, and as a general rule no days of grace are allowed. On the due date the payment of the hundi is made by the drawee to the holder thereof. The drawee of a hundi is the party primarily liable to pay the amount, while the drawer and each endorser stand in the position of sureties. The dishonour of hundis is an event of rare occurrence. If a hundi is not honoured on the due date, the drawer is considered to be insolvent, and it is a common practice for the holder to give to the drawee an intimation of its dishonour by means of a telegram. Then the eventual remedy of the holder will lie in a court of law.

If the original hundi called *khoka* is lost, a second copy called *paith* is issued; and if even the second is lost, a third called *parpaith* is given.

Hundis provide the most convenient method of obtaining funds for business purposes at a very reasonable cost, provided the borrowers enjoy good credit and reputation in the trade. They also afford an excellent source of investment to those who have spare funds, but it is essential that the persons lending money on hundis should have a personal knowledge of the financial standing of borrowers, otherwise a loss may be sustained on account of the hundis being dishonoured.

II. Company Finance

Note:—The sections referred to in the following pages of this chapter are the sections of the Indian Companies Act of 1913.

Businesses which need large amounts of capital are usually organised on the joint stock principle, because a joint stock company is a very good device for raising capital from the public. The division of a company's capital into smaller units makes it possible to attract funds from persons of small means; and it also enables investors to diversify their investments in a number of companies thus reducing the risk of loss. By issuing securities of different forms such as *preference shares*, *ordinary shares*, *debentures*, etc., a company can appeal to persons of different temperaments and different economic position. The fact that the securities of a company can be easily marketed through the mechanism of stock exchanges makes it possible for investors to withdraw their funds if necessary. Finally it is the privilege of limited liability which facilitates the raising of huge amounts of capital from the public.

It is a well-known fact that before a public company can be started a certain amount of preliminary work has to be done involving the expenditure of both money and talents. The person who does all this preliminary work is known as the 'promoter'. A promoter is therefore one who plans a venture, settles the constitution of a company and procures its registration and takes the necessary steps to attract capital from a body of investors. The work of the promoter may commence long before the company is formed and it may continue after the necessary capital has been obtained.

If a company is being formed to purchase an existing business, one of the first steps taken by its promoter will be the opening of negotiations with the vendors in order to secure their approval to a draft scheme under which they give the promoter an option to purchase their business at a definite price on behalf of the proposed company. The promoter will then arrange the preliminary finance and determine the general powers which are to be taken by the company under the memorandum of association. The internal arrangements of the company will be set forth in the articles of association. A suitable name will be selected for the company and the necessary documents will be prepared and filed with the Registrar. Of course, the promoter will have to decide what the authorised capital of the company is to be and provide the money for the payment of charges associated with the registration of the company. The promoter of a company may be paid for his services by cash or a free issue of shares, but in this country he is usually rewarded by being entrusted with the managing agency of the company which he has created.

Capital Structure

The most difficult problem with which the promoters of a company have to deal is the arrangement of its capital structure. There are two distinct aspects of the capital scheme, viz. the total amount of the capital required and the ways in which it may be raised.

Measuring Capital Requirements. Every company requires capital for two purposes: (i) Capital for block, that is to finance fixed assets and expenses of organisation, and (ii) Working capital, that is, to finance floating assets. Block capital or construction capital is required for purchasing land, buildings, machinery and other appliances of a permanent and durable character and also for formation expenses. In the case of established companies it may also be required for purposes of extensions and improvements. The capital that is invested in these assets is more or less of the nature of permanent investment.

Working or trading capital, on the other hand, is required for the purchase and working up of raw materials into finished products, for stores, for expenses incidental to the marketing of products for financing outstandings in respect of goods supplied and for providing the necessary funds for meeting the day to day requirements.

The relative proportion between block and working capital required for a company varies with the nature of the business. In the distributive trades and in cottage industries where the fixed assets are comparatively inexpensive and few, the fixed capital is very small as compared with working capital; while, on the other hand, in modern industries, the proportion of block to working capital is much larger. Again, as the processes of production become more and more roundabout, the proportion of fixed to working capital increases correspondingly.

In order to arrive at the amount of working capital needed, the following

matters must be taken into account : (a) The period which will elapse before the factory will be producing saleable products ; (b) The amount required to finance production during such period, e. g., in respect of raw materials, stores, wages and overhead expenses, having regard to any credit obtainable : (c) The period of credit allowed to and by the business, and the probable amount of debts outstanding, both by and to the company after production has started ; (d) The estimated turnover having regard to periodical fluctuations ; (e) The estimated outlay on wages and expenses after production has started ; and (f) The average stocks required, both of raw materials and stores and finished goods, and the amount of work-in-progress.

The capital raised by a new company should be sufficient for efficient and economic working of the enterprise. The amount of capital required for a new business depends upon its size. The promoters must, therefore, first of all decide upon the size of the proposed enterprise. Perfect technical knowledge is essential for a correct decision in this respect. Once the size is decided upon, the financial estimates become comparatively an easy matter. The correctness of the estimates regarding the size and costs depends upon the efficiency of the promotion services. But in India where the promotion services are deficient, the estimates are likely to go wrong. One peculiar feature in this respect is that the Indian promoters generally err on the side of insufficiency of initial capital estimates.

The initial capital plans of Indian companies, as a rule, do not include working capital requirements. The permanent capital raised at the beginning is just enough for block purposes. The miscalculation about capital requirements is a common malady from which the Indian companies suffer. Theoretically speaking, the permanent capital (shares and debentures) should suffice both for block and current requirements ; but this is seldom the case in practice. In forming a capital plan with a view to starting a company on a secure foundation how much of the estimated working capital of the concern should be raised by shares and debentures and how much of it may be secured by way of short-term finance ?

The answer is that a certain portion of working capital, although used for current expenditure, is in reality of the nature of permanent finance. The stock of raw materials, manufactured and semi-manufactured goods and of stores never falls below a certain minimum, and therefore the capital required for holding them is of the nature of permanent capital. Only that amount of working capital over and above this minimum falls under the category of short term finance. The mistake of most of the company promoters in India lies in thinking that the whole of the working capital is in the nature of a fluctuating demand for credit, varying with the demand for the products of the company. It has to be made clear that it is not sufficient in itself that a company should put up its block from its own capital and that, having done so, the company can appeal to the banks for loans and assistance. Not only

block but also normal working capital has to be furnished out of the company's own initial capital.

Form of Capital Structure. When the amount of capital required for the business of a company has been estimated the next thing to consider carefully is the form in which it should be raised. The necessary capital may be obtained by means of shares (either of one class or of several classes such as preference, ordinary or deferred), debentures and/or public deposits. What factors determine the class or classes of shares to be issued or as to whether a portion of the capital should be raised by debentures or public deposits? The factors regulating this question are as follows :—

1. *Requirements of Potential Investors.* A company issues securities of different types in order to cater for as large a number of investors as possible. All investors are not of the same nature; some are very cautious, some less so, while others are venturesome. Again, some shareholders have large amounts of money available for investment which they can easily afford to risk, while others having only a moderate and hard-earned saving will think ten times before investing it. Thus the investors widely differ in temperament and economic position. The various types of securities that a company may offer to the public are therefore designed to meet the wishes of different types of investors.

2. *Nature of Company's Business.* The nature of a company's business is an important factor in deciding upon the form of capital. Of course, the necessary capital should, if possible, be raised by the issue of securities of different classes, but all companies are not in a position to do so. Preference shares can be issued only by those companies whose earnings are almost assured, e.g., jute mills, sugar mills, public utility concerns and the like. Where the business is of such a nature that it has a large amount of readily realisable assets and earnings with little variation, it is easily in a position to issue debentures. A company, desiring to issue preference shares and debentures, must be engaged in a business which is not of a speculative nature and whose profits are deemed to be sufficient for the payment of preference share dividends and debenture interest regularly. If the business is of a speculative nature or liable to acute fluctuations or has not yet been established on a revenue-earning basis, a large proportion of the capital—preferably the whole of it—should be in the form of ordinary shares.

3. *Money Market Conditions.* The state of the money market has also to be taken into account in fixing the form of the capital structure. At some times happens that the investing public is anxious to invest safely; at other times the general desire is to obtain shares which offer the possibility of high return and capital appreciation. In times of depression, with money rates low, a debenture issue is much more likely to be successful than a share issue. Moreover debentures can then be issued at low rates which will be of distinct

benefit to the company when trade revives. When a trade boom is in progress, shares can be issued often at a high premium. In such circumstances, it would be a bad policy to issue debentures, for these would have to be given high interest rates.

4. *Desire to Retain Control.* Sometimes the capital structure of a company is so designed as to concentrate control in the hands of a group of individuals. It may be that the company is being formed to acquire an existing business and additional capital is required for its development. If the vendors are to be the persons responsible for the conduct of the company's affairs, they may not themselves be in a position to provide these funds and they must therefore make an appeal elsewhere. They naturally do not wish to share the control with others if it can be avoided and consequently they may decide to issue preference shares carrying restricted voting rights. A good many investors are quite satisfied to sacrifice such rights in return for the advantages as to dividends and or return of capital which preference shares usually enjoy. A similar course is also sometimes adopted by promoters who are not slow to take advantage of the opportunity of controlling large concerns with a minimum use of their own funds. This is secured by issuing deferred shares of small value carrying disproportionate voting rights.

5. *Cost of Capital.* If a company raises the whole of the capital required by issuing shares of one class only, the remuneration to be paid thereon will be higher than when it issues securities of different types, because the return expected by investors on ordinary shares is higher than that on preference shares or debentures. Suppose in a certain company the investors expect a return of 10 per cent. on ordinary shares, 6 per cent. on cumulative preference shares and 5 per cent. on debentures, and the company is in need of a capital of Rs. 10 lakhs. If the entire capital consists of ordinary shares alone, the company must find Rs. 1,00,000 profits to pay the expected dividend; if Rs. 4 lakhs is raised by 6% Preference shares and the balance by ordinary shares, a profit of Rs. 84,000 would be sufficient to pay the desired dividends; and if the required capital is obtained as to Rs. 4 lakhs by ordinary shares, Rs. 3 lakhs by preference shares and the balance by means of debentures, the company would require a sum of only Rs. 73,000 to satisfy all of the investors. It is therefore more economical from the point of view of the company if the entire capital is issued in the form of different kinds of securities.

6. *Elasticity of Capital Structure.* When devising the capital structure of a newly-formed company, it is essential to take into consideration not only its present financial needs but also its future financial requirements. The corporate organisation is intended to go on. Immediate financing is, of course, important, but the future must not be lost sight of. As the business grows and expands, it will need more and more capital. As the present debenture issue becomes due, fresh finance will have to be obtained for its redemption. Therefore the capital structure must be elastic so as to permit the raising of

further capital without any difficulty. It means that provision should be made for future financing by having substantial amounts of authorised but unissued capital. The fixed charges of the company should be kept well within its earning power so that the new issues of capital may be readily saleable. In some companies debentures are not issued at the beginning; so when an emergency arises mortgage debentures can be issued to obtain new funds. Other companies simply do not use their full borrowing power during normal times.

7. Gear Ratio The factor of gearing requires careful consideration in connection with the capital structure. The term "Gearing", when applied to the capital of a company means the relationship of the ordinary share capital with the total capital and it is said to be high or low as the former is small or large compared with the latter. For example, if out of a company's total capital of Rs. 10 lakhs the ordinary shares have provided only Rs. 3 lakhs, the balance being in the form of preference shares and debentures, then the share capital of the company possesses a high gearing, and the ordinary shares are said to be highly geared. The higher the gear, the more speculative the ordinary shares. It is of the utmost importance that a proper proportion is maintained between the amount raised by ordinary shares and that raised by preference shares and debentures. As the gearing increases, the value of both the priority rights and the ordinary shares decreases, and so does the credit of the company, if under such circumstances the dividend on the ordinary shares is not paid by the company. Moreover, care should be taken that too much capital is not raised by way of debentures, because debentures do not share in business losses.

8. Mutual Rights. Where it is decided to raise the capital required by means of securities of different kinds, the rights attached to each class of security must be reasonable. The rates of income to be attached to preference shares and debentures should be determined by studying the yields of similar securities in the market at the time the issue is brought out. The terms of repayment of debentures (and preference shares if they are redeemable) should be well within the capacity of the company and the voting rights attached to different classes of shares should be fair.

Raising of Capital. When the amount and the form of the capital of a company have been decided upon, the promoters take the necessary steps to procure it either privately or by public subscription; and if the latter course is adopted, a prospectus is usually necessary. An appeal for the necessary capital is made to the public by means of the prospectus, which has already been fully discussed in a preceding chapter.

The various ways in which a public limited company obtains the necessary finance are:

- (a) Issue of Shares,
- (b) Issue of Debentures;
- (c) Bank Loans;
- (d) Loans from Managing Agents; and

(c). Public Deposits.

Each of these methods will now be considered in detail.

(a) Issue of Shares

The amount of capital which a company may raise by means of shares is stated in its memorandum of association, in which the number of shares into which such capital is to be divided is also mentioned. But the classes into which the shares are to be divided are fixed by the company's articles of association. It is not necessary that all the shares a company is authorised to issue should be so classified. Some of them may be classified and some may be left unclassified to be issued as a particular class in future by the directors of the company.

The three principal classes of shares are preference, ordinary and deferred shares, but there may be several variations of them. The respective rights and privileges of each class of shares in a company are found in its memorandum and/or articles of association.

Preference Shares.

These are shares that carry with them certain preferential rights in priority to other classes of shares, and that is why they are called preference shares. The several rights and privileges attached to preference shares may be as follows :—

1. *Dividends.* The preference shares have a prior right to a fixed dividend, i. e., dividend on other classes of shares are deferred until the fixed dividend is paid on the preference shares. Unless the articles provide to the contrary, preference share dividends must be paid less tax; the declaration of free of tax dividends would deprive ordinary shareholders of profits to which they are entitled.

The fixed dividend on preference shares may be paid yearly or half-yearly. The existence of profits sufficient to pay the fixed dividends does not, of itself, give preference shareholders a claim to such dividend. If in the directors' discretion it would seem that allocations to general reserve or other purposes are in the best interests of the company, they are justified in passing the preference dividend, or recommending its payment in part only. But directors must act in the interest of the company as a whole; any attempt to defeat the claims of preference shareholders by this means would be nullified if the members concerned obtained an injunction restraining them from disposing of profits in the proposed manner.

Preference dividends may be paid in a year when a loss has been incurred, provided undivided profits carried forward from previous years are adequate to meet the payment, that is to say, a sufficient balance of past profits remains for the payment of the preference share dividend after making good the current year's loss.

The dividend attached to preference shares may be cumulative, non-cumulative or partly cumulative and partly non-cumulative. If the preference

share dividend is cumulative and if it is not paid in full in any one year or for a term of years, it must be paid up in full before the other shareholders can share in the profits. But where the preference share dividend is not cumulative, it extends only to each year. Accordingly, preference shares are known as cumulative or non-cumulative preference shares. The preference share dividend is usually cumulative.

2. *Repayment of Capital.* Almost invariably preference shares carry the additional right to a return of capital in priority to other classes of shares; but this right is not available unless expressly conferred by the articles. In the absence of any express provision to this effect, preference shares rank, on winding up, equally with other classes in the matter of repayment of capital.

3. *Participation in surplus profit and assets.* Sometimes, especially in the case of companies working a rather speculative class of enterprise, preference shareholders, after receiving the full dividend to which they are preferentially entitled, have also the right to a further share in profits after the ordinary shareholders have received a certain amount of dividend. A preference share having such a right is called a cumulative participating preference share. Such a share is very strongly protected. It carries the right to a fixed dividend before the ordinary shareholders receive anything, so that if the company is only moderately successful its service has to be considered first and at the same time if the company earns big profits it gets some further share in them after the ordinary shareholders have had their slice. This form of preference share is not, however, common. Preference shares are, however, entitled to their proportionate share of any surplus assets on winding up, after arrears of dividend, if any, have been met and all capital repaid, unless that right has been expressly or by clear implication taken away. This is the legal position; but in practice companies usually issue preference shares subject to a provision which entitles them, on winding up, to priority as to repayment of capital and arrears of dividend up to the commencement of winding up over other classes, but no further right to participate in profits or assets.

4. *Right at General Meetings.* The rights of preference shares with regard to the receipt of notice of, and to attend and vote at the general meetings of the company are governed by the articles. Preference shares may have equal voting powers with ordinary shares, but it is usual to restrict the preference share voting power, and frequently to withhold voting right until the dividend is in arrear.

5. *Right to appoint directors.* Occasionally, in order to make preference shares more attractive to investors, it is provided that the preference shareholders shall have the right to appoint one or more directors of the company.

6. *Restriction on Creation of Prior Rights.* A company which has already issued preference shares may make a future issue of capital having priority over the existing preference shares. The new shares will then be known as 'pre-preference shares'. Unless the preference shareholders' rights are properly

safeguarded in this respect by a suitable provision in the company's memorandum or articles, the company may create shares having prior claims to dividends and capital without consulting the existing preference shareholders whose interests are prejudiced.

7. *Right of Conversion.* Where a right of conversion is attached to preference shares, the preference shareholders can convert them into another class of shares, e. g., ordinary or deferred within a specified time. The right of conversion is usually attached to redeemable preference shares. Where preference shares have the right of conversion, they are called convertible preference shares.

8. *Guarantee Right.* Preference shares issued by a company may be guaranteed as to dividend and repayment of capital by another company. Guaranteed preference shares offer to the investor additional security.

9. *Redemption Rights.* A company issuing preference shares may undertake to redeem them after a specified period or after giving a specified notice. Such preference shares are called redeemable preference shares. Redeemable preference shares may very appropriately be issued by a company in the following circumstances:—(a) When semi-permanent finance is to be raised, preference shares may be issued with an option for the company to redeem them after a specified period; (b) When, in times of high interest rates, the long view suggests a lower rate, the issue of redeemable preference shares is very appropriate, because full advantage can be taken of subsequent conversion to lower rates; and (c) When a company capitalises its profits, the bonus shares can very properly be issued in the form of redeemable preference shares, so that, if necessary, they may be redeemed out of future profits.

It is, however, possible to a certain extent that the power to issue redeemable preference shares may unfavourably react against the raising of preference shares capital, as shares which the company has power to redeem in the event of money rates falling would not commend themselves to every investor. But in order to compensate the preference shareholders for their possible loss of income on redemption and provide an additional inducement to invest in the issue, such shares may be redeemable at a premium, or there may be attached to an issue of redeemable preference shares an option for the holders to take up at par or at a fixed premium shares of another class. In the event of the initial capital expenditure becoming fully productive by the redemption date, the right of conversion may be of considerable value and would more than compensate the holders for a possible loss of income on redemption.

On the other hand, it must not be overlooked that redeemable preference shareholders possess a reasonable assurance that their capital will be repaid at the price determined at the time of issue, and the risk of depreciation in the value of their shares is accordingly diminished.

Ordinary Shares.

The ordinary shares are those that rank for dividend and capital repay-

ment after the preference shares, but (unless there are deferred shares) they take the whole of profits remaining for distribution after the fixed preference share dividends have been paid. They give to the owners not only a varying dividend prospect but also the opportunity of capital appreciation on market values.

Preferred Ordinary Shares The holders of these shares have the right to a non-cumulative fixed dividend after the claims of the preference shareholders have been met and before the ordinary shares rank for dividend. Preferred ordinary shares thus occupy a position between the preference shares and the ordinary shares, or where no preference shares have been issued, they have the same status as preference shares.

Deferred Shares.

The deferred shares rank for dividend after all the other classes of shares have received fixed rates of dividend. They are generally few in number and small in nominal value, but the voting powers which they command and the profits to which they are entitled are often considerable.

Advantages and Disadvantages of Shares

From the point of view of the company, there are a number of advantages and disadvantages of obtaining capital by means of shares, and these are:—

Advantages 1. No charge of any kind is created on the assets of the company, therefore they remain available for any further financing by means of borrowing.

2. Dividends are not payable save out of available profits of the company. Even if there are profits, dividends on shares (whether preference or ordinary) may be passed if in the opinion of the directors such a course is in the best interests of the company.

3. Where recent profits of the company have been consistently high, further capital can be raised on very favourable terms by the issue of ordinary shares.

4. There is no obligation to repay the amount of share capital during the lifetime of the company except in the case of redeemable preference shares and even the redemption of redeemable preference shares is so safeguarded by law that the finance of the company will not be adversely affected by such redemption.

5. The cost of capital will be comparatively less if the shares issued are preference shares.

Disadvantages. 1. A share in the equity of the company is, by an issue of ordinary shares, given to the new shareholders.

2. A comparatively higher return is payable on ordinary shares.

3. Since the constitution of the shareholders of a company is constantly changing, the new shareholders may tend to influence the existing policy of the company.

4. If it is desired to increase the authorised share capital of the company, the sanction of the shareholders is necessary, and if an issue with any

special rights is contemplated the consent of a specified majority of the existing shareholders will be required, which may not be easy to secure.

(b) Issue of Debentures

A trading company has an implied power to borrow, if such borrowing is properly incidental to the conduct of its business. Such power is, however, expressly taken in the memorandum of association. In the case of a non-trading company the law does not give an implied power to borrow. A non-trading company must, therefore, have express power in its memorandum before it can borrow. When a company can borrow it can also pledge its property as security. A limit is usually placed on the amount to be borrowed either by the memorandum or by the articles.

A company may pledge the whole of its property and undertaking, both present and future, as security for loans, where it has an express or implied power to borrow. If it desires to pledge its uncalled capital it must have express power in its memorandum or articles to do so. The uncalled capital cannot, however, be pledged under any circumstances, where it has been specially earmarked as reserved capital under section 69 of the Indian Companies Act; nor can a banking company, under section 277-J create any charge upon its uncalled capital.

The articles of association of a company will provide whether the power to borrow is to be exercised by the company in general meeting or whether the power shall be vested in the directors. The usual plan, however, is for the directors to be authorised to exercise the borrowing powers of the company up to a certain limit, and that limit is not to be exceeded except with the sanction of the company. The limit may be the amount of the nominal capital of the company for the time being or any other amount. Under section 87-G of the Indian Companies Act, a managing agent cannot exercise in respect of any company of which he is a managing agent a power to issue debentures.

Section 103 of the Indian Companies Act provides that a company cannot exercise its borrowing powers until it has received a certificate entitling it to commence business, but that a company may nevertheless, before it obtains such a certificate, offer shares and debentures simultaneously for public subscription, may allot shares and debentures and receive money payable on application for debentures. This restriction does not apply to private companies which may exercise their borrowing power as soon as they are incorporated.

A company may borrow in the shape of short-term or long-term loans according to its needs. Short-term loans are usually taken from banks; but long-term borrowing may be either by means of mortgages on its property or, as is more usual, by an issue of debentures.

Debentures. A debenture is a mere acknowledgment of indebtedness given under the seal of the company containing a contract for the repayment of the principal sum at a specified date and for the payment of interest (usually half-yearly) at a fixed rate per cent. until the principal sum is repaid, and it

may or may not give a charge on the assets of the company as security for the loan.

Many forms of debentures exist, and the term is somewhat loosely applied in business, but the following observations should be read in conjunction with the foregoing definition :—

1. A debenture, as a rule, is one of a series which are expressed to rank *pari passu* with each other as to any charge given by the debenture. If the debentures of a series are not made to rank *pari passu* they would rank according to the date of issue or if issued on the same day in numerical order. The company cannot create new series of debentures to rank *pari passu* with the old, unless the right has been specifically reserved.

2. Debentures are not confined to companies alone, but clubs, municipal corporations, port trusts and other public bodies very often issue them.

3. Debentures usually provide for the repayment of the principal sum on a fixed date, usually five, ten or twenty years after issue, or they may be repayable on demand, or they may be irredeemable. They can be made perpetual in the sense that there need be no fixed time for paying them off. Section 126 of the Indian Companies Act permits the issue of irredeemable debentures, although in practice such debentures are unknown.

4. The rate of interest payable is usually specified to be at a fixed rate per cent., but it need not be so. The capital sum may carry no interest and the debentures may be issued at a discount and the capital sum be expressed to be repaid at par or at a premium. The interest payable may also be made to vary with the profits, or provision may be made in the debenture to the effect that the interest shall only be payable out of profits and such interest may be cumulative or non-cumulative.

5. Debentures may or may not give a charge on the property, assets or undertaking of the company. Where they do give a charge they should always be referred to as Fixed Mortgage Debentures if the charge is fixed or Floating Mortgage Debentures if it is not fixed.

6. Debentures giving a charge on the property of the company may or may not also be secured by the creation of a trust deed vesting the property in trustees upon trust, such trustees having power on the default of the company to sell the assets and pay off the debentures.

Debenture Stock. Debenture stock is a term used to denote the capital sum lent to a company which is usually secured by a trust deed creating a mortgage or charge in favour of the trustees upon the property forming the security. The capital sum or stock is by the terms of the trust deed divided into units, in respect of his holding of which each stockholder is entitled to a certificate. The trust deed provides for a register of holders being kept, and for transfers of the stock in certain fractions, and usually contains provisions for repayment of the stock and for enforcing the charge. The incidents of

debenture stock are for practical purposes the same as those of debentures and the holders of the stock occupy a position very similar to that of the holders of debentures.

Status of Debenture-holders A debenture holder is a creditor of the company, and is entitled to interest at a specified rate whether profits are earned or not except when he holds what is known as an income debenture in which case interest is payable only out of profits. He therefore differs from a shareholder in that the latter is a member of the company whose income comes solely out of profits. A debenture holder usually possesses a security for his loan whereas a shareholder has no security. A debenture holder is not, however, entitled to anything more than his fixed interest, however big the profits of the company may be.

Security for Debentures. A company may issue debentures without any security (known as naked debentures); but usually a company's assets are charged as security in favour of the debenture holders. The security may be in the form of a specific mortgage or a floating charge or a combination of both.

When debentures are secured by a charge on the company's property, the charge may be created by words in the debenture itself, or by a deed the benefit of which the debenture holders are declared to be entitled to, or by a combination of both these methods.

Trust Deed. When debentures are issued for public subscription, a trust deed is invariably executed in favour of the debenture holders, a trustee or trustees being appointed and remunerated by the company to act on behalf of the debenture holders. The trust deed contains, *inter alia*, the following clauses:—

1. Particulars of the property charged as security, and whether by specific mortgage or floating charge or both.
2. Whether the company shall have power to create any mortgage having priority to the charge included in the deed.
3. Provision for redemption of the debentures, including the price and date or dates at which they shall be redeemed, and whether by drawings, by purchase in the market, or by ordinary redemption. If a sinking fund is to be created out of profits to provide for redemption, details of this will be included in this clause.
4. Powers of trustees to deal with the assets charged as security in the event of default by the company in payment of interest or repayment of capital or upon a winding up.
5. Whether the debentures shall be registered or in bearer form and the manner of their transfer.

When a trust deed is in existence, the debentures themselves should contain a clause incorporating its terms by reference. By section 125 (2) every debenture holder has the right to a copy of any trust deed for securing the debentures on payment of a sum not exceeding one rupee in the case of a printed trust deed or on payment of six annas for every hundred words required to be

copied where the trust deed has not been printed.

The trustees appointed by the company to look after the interests of the debenture holders may be individuals or a corporate body. Banks, share brokers, insurance companies and investment trusts usually act as trustees.

The most important advantages to be obtained from securing the debentures by the creation of a trust deed are :—

1. The property charged actually vests in the trustees ; and
2. The trustee can enter and sell the property charged immediately on default and can continually watch over the interests of the debenture holders and, if necessary, force the company to keep the property charged in good condition. In the absence of trustees, valuable time is usually lost by waiting for some debenture holder to take action.

It is clear that for the absolute protection of the security in the case of a fixed charge the title deeds of freehold property or leases (if the property is leasehold) should not remain in possession of the directors, since further charges ranking in priority to the debentures might be created. It is not possible, however, to give the security to each debenture holder and trustees are therefore appointed to represent them.

The trustees must carry out their duties under the trust deed honestly and must not commit any breach of trust therein contained, for they have the liability of and are in the same position as other trustees. They are appointed and their remuneration is fixed by the deed. If no provision is made in the deed for remuneration they are not entitled to any.

Under section 146 of the Indian Companies Act, the trustees for debenture holders have the same right to receive and inspect the balance sheets and profit and loss accounts of the company and the reports of the auditors and other reports as is possessed by the holders of ordinary shares in the company.

Fixed Mortgage. A fixed charge consists of an actual mortgage of the assets of the company usually to trustees for debenture holders, thereby preventing the company from creating charges in priority to the fixed charge.

The fixed charge is usually restricted to what are known as fixed assets. The company cannot deal with the assets that have a fixed charge upon them. No fixed charge is, therefore, created on floating assets of the company.

Floating Charge. Debentures may be issued giving a floating charge on the assets and/or undertaking, both present and future, of the company as security for the debentures.

A floating charge does not prevent the company from dealing with the property so charged in the ordinary course of business. It may embrace moveable property as well as fixed property, and the property so included may change its character in the conduct of the company's business. For example, stocks will automatically change into debtors' balances and cash ; debtors' balances will liquidate into cash, and cash will be expended in new stocks, etc. Uncalled capital and future property are frequently contained in the charge.

Not until a floating charge becomes fixed (or as it is often termed 'crystalises') is the company precluded from disposing of the assets involved. The circumstances in which a floating charge crystalises (a. g., failure on the part of the company to pay interest on the due dates or neglect to satisfy the provisions as to redemption) are enumerated in the debentures or the trust deed.

Fixed v. Floating Charges. The advantage of a fixed charge over a floating charge lies in the fact that the debenture holders know to which particular assets they may look for security, if need arises. Against this, the security afforded is restricted to specific assets which may shrink in value. Buildings erected for the special purposes of the business are often saleable only at a considerable loss.

When debentures are secured by a floating charge, the holders may rely upon any assets included in the charge for the satisfaction of their claims, even though certain assets may not have been in existence at the time the charge was created. On the other hand, a risk is always present that in the event of a prolonged period of depression ensuing, a company's assets may become partially consumed in an attempt to avert financial disaster. This eventuality would result in a contraction of the security furnished by a floating charge. The widest security is not therefore necessarily the best, and each should be valued on its merits.

A floating security is an equitable charge on the assets for the time being of a going concern; it attaches to the subject charged in the varying condition in which it happens to be from time to time. It is the essence of such a charge that it remains dormant until the undertaking charged ceases to be a going concern, or until the person in whose favour the charge is created intervenes. His right to intervene may, of course, be suspended by agreement. But if there is no agreement for suspension he may exercise his right whenever he pleases after default.

It is important for investors to remember that floating debentures do not give a paramount security for the following reasons:—

1. The company is free to create specific mortgages on the property charged in the floating debenture having priority over such debenture unless otherwise agreed in the terms of the issue of the floating debenture that the company shall not be at liberty to create any charge having priority over them.

2. By section 233 of the Indian Companies Act a floating charge created within three months of the commencement of winding up will only be effective to the extent of the amount then actually advanced to the company with interest at five per cent. per annum unless the company was solvent at the time the charge was given.

3. Under section 129 of the Act, if a receiver is appointed in respect of debentures secured by a floating charge or possession is taken by or on behalf of such debenture holders and the company is not in the course of winding up, then the receiver or other person taking possession must pay out of the assets

coming into his hands the debts which are by section 230 preferential in priority to the principal or interest in respect of the debentures.

The difference between a fixed and a floating charge is clearly brought out in the following extract from a judgment:—

'A specific charge, I think, is one that without more fastens on ascertained and definite property or property capable of being ascertained and defined; a floating charge, on the other hand, is ambulatory and shifting in its nature, hovering over and so to speak floating with the property which it is intended to affect until some event occurs or some act is done which causes it to settle and fasten on the subject of the charge within its reach and grasp.'

Issue of Debentures. Debentures, unless privately taken up by the managing agents, directors and their friends, are usually offered to the public by means of a prospectus, which must include all the information relevant to company and to the debentures as required by section 93 of the Indian Companies Act.

Debentures may be issued to a creditor in respect of an existing debt or a fresh loan or as collateral security. They are, however, usually offered for public subscription in the same way as shares and afford a prospective investor an alternative form of investment in the company.

They may be issued like shares at par, at a premium or at a discount. Sometimes debentures may be issued at a considerable discount but no interest may be payable thereon for some time. Thus Belsund Sugar Co., Ltd., issued in 1931 Rs. 10,00,000 Debentures of Rs. 100 each at Rs. 80 per debenture, carrying no interest for the first two years but thereafter at the rate of 5½ per cent. per annum. The interest attached to debentures must be paid after deduction of income-tax, but a company may issue debentures carrying interest free of tax, in which case the income-tax on debenture interest will be payable by the company.

Where debentures have been issued at a discount and where any commission is paid on their issue, the following publicity has to be given to these facts:

Section 106 makes it obligatory for a company to show any sums paid by way of commission and any sums allowed by way of discount on debentures in every balance sheet until the whole amount has been written off.

Under section 111, particulars of any commission or discount paid on debentures must also be filed with the Registrar along with the particulars of mortgages and charges.

Any expenses incurred in connection with the issue of debentures so far as they are not written off, must be shown under a separate heading in the balance sheet.

N. B.—A contract with the company to take up and pay for any debentures of the company may be enforced by a decree for specific performance as laid down in section 126.

Registered and Bearer Debentures. A registered debenture is one whose holder is registered in the books of the company. The object of issuing registered debentures is to meet the requirements of the money market and to facilitate dealings. It simplifies the title and enables the company to look to some specific person as the holder to whom it can make payments, and whose receipt is to be a sufficient discharge.

Although a company is not bound to keep a Register of Debenture holders, yet in practice one is usually maintained in which to record the names, addresses, occupations and amounts of holding of each debenture holder. This register is dealt with and written up in the same manner as the Register of Members. If a register of debenture holders is kept, section 125 requires that it must be open to the inspection of members and debenture holders during at least two hours a day. There is a heavy penalty for refusing inspection.

Registered debentures are transferred in the manner specified in the conditions endorsed thereon—usually by means of a transfer deed. A company can become a transferee of its own debentures, and the same debentures may be reissued as explained later on.

Alternatively, a debenture may be in 'bearer' form, i. e., transferable by mere delivery. The interest due is paid to the holder irrespective of his identity, at each interest date. Coupons are frequently attached to bearer debentures for presentation through a bank on the due dates.

A bearer debenture is therefore possessed with the attributes of a negotiable instrument, i. e., its legal ownership passes by mere delivery, no written transfer being necessary to invest it in a purchaser.

Some companies issue bearer debentures in the first instance but they give to the holders the option of converting their debentures into registered ones if they so desire.

Redemption of Debentures. Under section 126 a company can issue ~~irredeemable or perpetual debentures but such debentures are almost unknown~~ in practice. Debentures are invariably redeemable, and the date on or before which they must be redeemed is stated in the terms of issue. The provision for the redemption of debentures is usually made by one or more of the following methods :—

1. On a specified future date, with an option entitling the company to redeem (either in part or in whole) on or after a stated earlier date.
2. By purchase in the market at or below a certain price either at any time, or on or after a specified date.
3. By drawings, either at fixed intervals, or at the company's option on or after a specified date.

In addition, the redemption may be at a price corresponding with the price of issue, or may be at a higher price, or may vary according to the particular option which the company may exercise.

The object of a company reserving to itself at least two alternatives, either

as to date or as to price, or both, is to enable it to choose the most favourable time to redeem the loan, having regard to the state of its own credit and external monetary conditions.

Convertible Debentures. In some cases an option is given to debenture holders to exchange their debentures for shares. Such a provision gives an investor the privilege of coming in with the status of secured creditor and retaining that relationship with the company until such time as profits appear to be sufficiently high to justify changing his status to that of a shareholder. He is thus able to retain the advantage of having his money secured on the assets until the company is in a sound financial position although it must be realised that once he has elected to exchange his debentures for shares, he has no right subsequently to revert to the capacity of debenture holder.

Registration of Mortgages. By section 109, every mortgage or charge created by a company and being either—

- (a) a mortgage or charge for the purpose of securing any issue of debentures, or
- (b) a mortgage or charge on uncalled share capital of the company, or
- (c) a mortgage or charge on any immovable property wherever situated or any interest therein, or
- (d) a mortgage or charge on any book debts of the company, or
- (e) a mortgage or a charge, not being a pledge on any moveable property of the company, except stock-in-trade, or
- (f) a floating charge on the undertaking or property of the company; shall, so far as it contains a charge, be void against the liquidator and creditors of the company, unless it is delivered for registration with the Registrar within twenty-one days of its creation.

In addition to the registration of mortgages and charges with the Registrar, the company must keep (i) a register of mortgages and charges specifically affecting the property of the company (section 123), and (ii) copies of all mortgages and charges which have to be registered with the Registrar (section 117). Section 121 further provides that both these shall be open to the inspection of any creditor or member without charge, and the register available for the inspection of any other person on payment of a fee not exceeding one rupee.

Advantages and Disadvantages of Debentures

Advantages. 1. It is easier to raise sufficient funds as it is possible to tap conservative people who desire a fixed income without much risk.

2. The fear that if too many ownership securities are issued the rate of interest on them may fall down is removed, as the return on the debentures is fixed leaving the rest for being shared by the owners.

3. If sufficient funds are raised by debentures the difficulties that arise owing to dependence upon uncertain sources of capital such as public deposits and commercial banks are removed.

4. The debentures are more economical as the rate of interest on them is

certainly lower than the rate of interest on the short-term borrowings.

5. By issuing redeemable debentures the capital structure of a company can be kept low, so that, when any exceptional prosperity disappears, the company may not find it difficult to pay a reasonable return to shareholders. This will be the case if the company sets apart every year a sum from its profits as reserve for debenture redemption, the sinking fund being used for paying off a portion of the debenture debt every year. Such annual payments of debentures will gradually reduce the burden of interest and make available for shareholders a greater amount of profits.

Disadvantages. 1. Interest on debentures is payable whether or not there are profits.

2. Being secured against the assets of the company, they affect its credit in the money market. The result is that banks which supply short term finance to companies curtail their advances.

Debentures in Company Finance. The use of debentures as a means of raising a part of the long-term finance required by a company is very desirable also, as it ensures economy; but all companies are not in a position to do so. Before a company can issue debentures it must have sufficient tangible assets to offer as security and it must have large and certain earnings to pay the regular debenture interest. If its earnings are likely to fluctuate greatly from year to year, it cannot afford to raise much capital by way of debentures.

There are two kinds of industry which can appropriately issue debentures. When the property of a company is of a non-specialised character and can be put to a variety of uses, such property furnishes the best security for the loan. Where the property of a company is specialised but it belongs to an industry which can be reasonably certain of relatively stable earnings, as most of the monopolies are, it can furnish the security for debentures. Railway, tramway and electricity supply companies belong to this class and their debentures are taken up in the market because of their earning power.

If the business of a company is of a speculative nature, it should not ordinarily issue any debentures. Care should be taken that too much capital is not raised by way of debentures, since constant interest credit which does not share in business losses, e.g. debentures and mortgages, become a danger to the very existence of an industrial enterprise. Moreover, interest on debentures and other fixed charges should be at a reasonable rate, and the terms of repayment of debentures should be well within the capacity of the company.

Why Debentures are not common in India. Debentures as a means of raising long-term company finance are not as popular in India as in other countries, and the reasons for this state of affairs are as under:—

1. **No Free Market.** The market for debentures in India has been rather limited. The Indian investor, if he wants safety, still plunges for agricultural landed property and is unwilling to take up industrial ventures unless there is a chance of capital appreciation. Hence debentures with a fixed yield of

interest and with no prospect of capital appreciation do not attract him.

Institutional investors such as banks, insurance companies and investment trusts do not take up industrial debentures. Insurance companies are not as a rule in a position to invest their funds in debentures owing to the restriction imposed by section 27 of the Indian Insurance Act of 1938, while commercial banks, following the lead of the Imperial Bank of India, do not favour debentures as a means of investment. Whatever investment trusts we have in this country are all of very recent growth.

The heavy stamp duty on debentures and on their transfers restricts, to a certain extent, the creation of a free market in them. For example, in Bombay the stamp duty on a debenture transferable by endorsement or by a separate instrument of transfer is Rs 7-8-0 per thousand rupees. On each transfer there is an additional duty of a similar amount. In the case of bearer debentures, there is an initial duty of Rs. 15 per thousand at the time of issue, but there is no additional duty on each transfer which is effected by mere delivery of the debenture.

The initial stamp duty of Rs 7-8-0 per Rs. 1,000 on debentures which are transferable by endorsement and Rs 15 per Rs. 1,000 on bearer debentures incurred by the company which issues them is left to be a burden, and the costs of transfer which fall on the investor are considered to be a handicap to effecting easy transfers.

Moreover, the small size of most of the debenture issues prevents the creation of a real market for them. The jute mill debentures are an exception. Not only are they popular, but they are considered to be so safe an investment that very few transactions are reported on the Stock Exchange. In regard to some of the debentures floated in Bombay, they are mostly taken up by limited groups of financiers and do not usually come to the market. Hence the public in Bombay has not become accustomed to the buying and selling of industrial debentures. When the Tata Iron and Steel Co., Ltd. issued debentures to provide itself with working capital, the entire sum of ₹400,000 (Rs. 60 lakhs) was subscribed by one Indian Prince, the Maharaja of Gwalior.

All debenture issues in India are usually of a very high denomination (Rs. 500, Rs. 1,000 and even Rs 10,000) and they are thus beyond the reach of the investors of moderate means. A low denomination debenture gives a double advantage to the investors with moderate means, because they cannot only invest their money in it with greater security but can also reduce their risks further by diversifying their investments.

2. *Attitude of Banks.* Perhaps the most severe handicap to the development of debentures in India has been the attitude of banks. A company which issues debentures find its credit weakened in the eyes of the banks. Its shares cease to be acceptable as collateral, and a company which is encumbered with a debenture loan has not the same credit with them as one without it. The

reason for this attitude is obvious. -Since debentures are a first charge on the property of the company, it is supposed that the security for bank credit is necessarily less.

3. *Terms Not Attractive.* There has been little variety in the nature of the industrial debentures offered to the market, and debentures with no special attractive features do not find favour with the investors. Other countries have known a great many forms of debenture issues, such as guaranteed debentures, debentures with a comparatively high premium on redemption, debentures having the right of appointing one or more directors of the company, debentures carrying the right to purchase ordinary shares at concessional rates, and so on. In a country like India where the capital market is not yet so highly developed it is all the more necessary that very liberal terms should be attached to debentures.

4. *Government's Fiscal Policy.* The fiscal policy of Government has been partly responsible for the lesser use of debentures in Indian company finance. When once an industry is started, the industrialist has no guarantee that he will be protected, if any such necessity arises, against unfair foreign competition. Therefore the investor in an Indian industrial undertaking has no assurance that the industry in which he invests will reach the profit-earning stage or that the profits, when once they accrue, will be maintained by inauguration of proper protective measures on the part of the Government of the country. Apart from the question of granting protection, there are, on the other hand, other Government measures to restrict the flow of capital into industry, such as the imposition of excise duties, anti national import policy with regard to consumption goods and so on.

5. *Heavy Expenses of Issue.* Debenture issues of industrial concerns have carried interest in India at varying rates not merely according to the soundness and credit of the concerns issuing them, but depending on the time of issue, the volume of issue and reputation of the underwriters. The interest is known to be anything from 5 per cent. to 9 per cent., and in addition to the interest there are the initial legal and stamp charges on the issue to be paid by the company, and there is the underwriting commission. Sometimes the issue price itself is below par.

6. *No Advisory Agencies.* There is no recognised method in India by which the general public can obtain advice and assistance as regards investments. No doubt banks' clients can obtain some sort of advice from their bankers, but there are many urban centres which do not still possess any banks and the assistance where it is available is not of the active, directing kind which banks in other countries supply to their customers for the advancement of industries. The Stock Exchanges function only in the large seaports and an up-country investor has little chance of getting in touch with any reliable or recognised member of these Exchanges.

Trading on Equity. A company may obtain a part of its resources by

borrowing, which may be long term, short term, secured or unsecured, formal or informal.

The company borrows money usually because it can use the borrowed funds to earn more than the rate of interest paid for the use of the funds. This practice is known as "*Trading on Equity*". The ordinary shareholders are the owners of the residual equity in a company. This equity is given as security to the lenders, who must be paid in full before the ordinary shareholders get back anything. It is because of the greater safety of his position that a lender is usually willing to take a lower rate of interest than the rate at which the company can employ the funds so obtained.

It must, however, be noted that sometimes a company has to borrow because that is the only way in which the necessary funds can be obtained. The shareholders are unwilling to put up more money, yet the business must have funds if it is to carry on. Borrowing is the only way out.

When further capital is needed and it is not desired to broaden the basis of ownership, an issue of debentures solves the difficulty, since the cost of the additional capital is exactly known. Should the prospects of expansion and good trade be excellent, an issue of loan capital is desirable. If the period of good trade arrives, then expansion can take place and the issue be redeemed out of accumulated cash reserves built up by withholding profits from distribution to shareholders.

The Underwriting of Corporate Securities

The practice of underwriting arose in connection with shipping ventures during the seventeenth century. The leading ship merchants of London were accustomed to assembling in Lloyd's Coffee House to transact their mutual business. In the course of time, the custom arose of dividing the risk of venture, some voyages among a number of different merchants, each one agreeing to stand a fixed share of the loss or to receive a proportionate share of the profits. The contract to this effect was passed about, and such merchant who agreed to it wrote his name under the contract—hence the word "underwriting". As is well known, the term is used chiefly in relation to the distribution of insurance risks, though when applied to industrial securities such as shares and debentures, the essential thought is the same, namely, that of distributing the risk.

Underwriting, as the term is used in corporation finance, is a method of sales insurance, whereby responsible persons (known as the underwriters) agree, in consideration of a commission either to purchase specified corporate securities in bulk for resale later, or, if these securities are offered by the company to the public, to purchase any balance of such securities not taken up by the purchasing public. In either case, the company is absolutely assured of the sale of its securities.

When a substantial company has been organised and its shares and debentures are to be sold, or when a company already in existence offers additional securities, the question of sale is one of paramount importance. When

industrial securities, are offered to the public, however sound an issue may be, there are always at work factors which may prevent a full response from the public. The investing public is capricious and does not always appreciate even the soundest undertakings. Subscriptions may also be scarce on account of another attractive offer being before the public, or because of the state of the money market. It would be fatal to a company trying to raise finance if its appeal for funds left it inadequately supplied. To prevent such a catastrophe, the issue will be underwritten.

Advantages and Disadvantages. The company that issues underwritten securities is absolutely assured, no matter what the conditions of the money market, that its money will be available at the agreed date or dates. The company can at once proceed with whatever projects the capital is designed to finance. There is no tedious and costly period of waiting during which the securities are in process of being sold. Many new enterprises are of such a nature that time is an important element in making them successful. If, for example, a new plant is being built in order to handle certain contracts, or, if an effort is being made to forestall competition, it might be fatal to the project if its inception were delayed until after all the securities had been sold.

The danger of discredit or of financial embarrassment from a failure to sell the securities is eliminated. Any unsold securities are quietly taken up by the underwriters, and the company pursues the even tenor of its financial way undisturbed.

The company gets the benefit of the specialised experience and judgment of the underwriters, and thus the risk of making a serious error in the form or in the price of the new securities is reduced to a minimum.

Not only is the underwriting device advantageous to the company, but also to the investors. In the first place, the fact that an underwriting has been arranged is in the nature of a guarantee that the security offered is sound. A still greater advantage is the insurance of the purchaser of the security against the same contingencies which would be harmful to the company; for it must be borne in mind that the moment the purchaser becomes a shareholder or debentureholder in the company, he begins to share in its good or evil fortunes. If the company, therefore, is injured by dragging out the sale of a new security issue over a long period or by bringing out a security issue which finally is not entirely disposed of, the purchaser of the securities is one of the sufferers. It is therefore, to his advantage that the issue should be underwritten and its success thereby assured.

It may therefore be stated that the cost of underwriting is well justified by the benefits received; and no one should grudge the expense involved in arranging for underwriting.

Underwriting Procedure. Two distinct plans are adopted in ordinary underwriting. Under the first plan the securities are offered to the public in the company which issues them. The underwriters then merely stand behind

the offering, undertaking to purchase the securities themselves if they are not purchased within a certain time by the public. Here the underwriters agree to become conditional purchasers of the securities.

Under the second plan the underwriters practically purchase the securities paying for them at such times and in such amounts as may be agreed. This is known as *'firm underwriting'*. The underwriters then either sell the securities at once, or hold them until such time as they can be disposed of to advantage. In either case the company has its money and is not further directly concerned.

Underwriting Commission. The commission payable to the underwriters is called underwriting commission, and it is payable on the whole amount of shares and debentures underwritten, irrespective of whether or not they are called upon to take up any of such shares and debentures under the agreement. It may be calculated according to agreement either upon the nominal value or the issue price of the securities underwritten.

The rate of commission payable for underwriting varies with the nature of the risk (i. e., the status of the company and the nature of securities), the state of the money market, and the fact whether the brokerage (if any) is to be paid by the company or the underwriter. If the brokerage is to be paid by the underwriter, as is usually the case when issues are underwritten, the commission will be correspondingly higher. It may range from 1%, to 10%.

Sub-underwriting If the underwriter does not wish to carry the whole risk on his own shoulders, he may transfer a part to someone else. This is called sub-underwriting, which is arranged by means of a contract made between the underwriter and the sub-underwriter, the company not being a party to it. The sub-underwriting is usually effected at a rate as much below the rate of underwriting commission as possible. If the underwriter agrees with the company to arrange for sub-underwriting, he is usually given an additional commission for such service known as *'overriding commission'*. Sometimes, however, in lieu of overriding commission the underwriting commission itself is increased.

Brokerage. When the shares and debentures of a company are offered to the public for sale, it is usually stated that the company will pay brokerage at a certain rate to bankers, brokers and other approved agents who procure buyers for its shares and debentures. The brokerage is paid in respect of the application forms bearing the brokers or bankers' stamp. Where the issue has been underwritten, brokerage may be borne either by the company or by the underwriters according to the underwriting agreement.

Why Underwriting Less Developed in India. In England and America most of the public issues are underwritten, but that is not so in India. This absence of underwriting may be attributed to the following causes :—

1. In England and America there are special institutions such as issue houses, investment trusts, finance companies, investment banks and the like, which undertake the work of underwriting industrial securities. In India there

have been till recently no such special agencies who could undertake this work. The absence of such institutions has been due to the infancy of joint stock enterprise in the country and the relatively small amount of the country's wealth invested in industrial securities.

2. Greater risks were attached to underwriting in India than in other countries, because here industrial securities did not command the confidence of the investing public on account of frequent company failures. Securities offered by good companies under able management did not need underwriting as they could be easily sold without its aid; while the securities of weak companies that needed underwriting did not appeal to those who could come forward to underwrite them.

3. The managing agency system itself has been a hindrance in the way of the development of underwriting. Before a person can come forward to underwrite the shares and debentures of a company, he will naturally examine the proposition, carefully weighing its chances of success, but this procedure in many cases is not liked by managing agents.

4. Managing agents are usually able, without underwriting, to go ahead with their capital plans, because of their own resources and also because of the confidence that they would be able to secure, in addition to the subscribed share capital, a considerable volume of public deposits.

However, the system of underwriting is now gradually improving and during the last fifteen years quite a large number of issues have been underwritten. The obstacles in the way of underwriting are now disappearing, and an increasing number of companies are now resorting to this device. The business of underwriting the shares and debentures of companies is done in India by promoters, vendors, managing agents, share brokers, commercial banks and investment trusts.

(c) Bank Loans

Generally speaking, the initial block capital required by public companies should be obtained by issuing shares and debentures. Further, an ideal arrangement is that companies should also provide their minimum working capital in the same way. The amount of minimum or normal working capital will depend upon the particular circumstances of each individual company. Any extra requirements of working capital over and above this minimum may be met by short-term advances taken from commercial banks, which are entitled to require that the company maintains a safe and proper relation between owned and borrowed capital. Moreover, such block capital required for subsequent improvements and extensions as is not provided out of undistributed profits should be supplied by increase of share capital or by an issue of debentures; but pending a favourable opportunity for such further issue of share or debenture capital, commercial banks may be expected to supply finance for these purposes in the form of temporary advances provided that adequate security is forthcoming.

The difficulties which Indian companies have to face in raising the neces-

any long-term capital have already been discussed. But the problem of company finance in India is not confined to the provision of long-term capital alone. The insufficiency of working capital and the high cost of such as is available are an important element in the problem of company finance in this country. The Indian commercial banks do not furnish finance for the fixed capital expenditure of companies, they merely provide current finance.

The principal directions in which Indian commercial banks supply current finance to companies are by discounting bills, advancing loans and granting cash credits. The short term bank loans are given to companies usually on the following terms :—

1. By far the greater part of the advances to companies is on the hypothecation or pledge of the stocks in trade. The difference between hypothecation and pledge may be noted. The stocks when hypothecated are stored in the godowns of the borrowing companies to which the banks are given access whenever they desire it, but the borrower furnishes periodical returns of stocks to the banks. The stocks that are hypothecated remain at the disposal of the company. The pledge of stocks, on the other hand, means that the stocks are placed in the custody of the bank with its name on the godown where they are stored, the company having no right to deal with them. Naturally a borrowing company will not like to pledge its stocks if it can avoid it, because the pledging of stocks is calculated to lower its prestige.

2. When loans are granted on the hypothecation of stocks, the bank also requires from the company a promissory note with two signatures, one that of the borrowing company and the other that of its managing agents. If the stocks are pledged to the bank, the personal guarantee of the managing agents is not required.

3. The loans and advances to companies are made for twelve months in the first instance, but there is an option for their renewal.

4. The rate of interest charged for loans and advances varies with the credit of the borrowing companies. For well-established companies the interest on the loans is at the prevailing Imperial Bank of India rate, but if the company is not very sound it may be required to pay one or two per cent. extra. In the case of cash credits banks sometimes insist on the half-interest clause by which the borrower has to pay to the bank interest on at least half the amount of cash credit in respect of the amount drawn.

5. Banks usually insist on maintaining a margin of about 30 per cent. in regard to advances against stocks and even a higher margin in regard to stocks in process of manufacture.

It will thus be seen that companies in India do not enjoy full banking facilities in the matter of raising finance. Banks do not make long-term advances to companies, and the short-term loans are made on very unfavourable terms. The following are some of the principal directions in which banks in India can make themselves more serviceable to companies :—

1. In connection with the issue of shares and debentures by companies, such of the existing commercial banks as are well-established and carry on their ordinary banking business on the safest and soundest lines might with advantage to the companies follow, as far as possible, the German system, a description of which is given later on. It is not, however, to the advantage of either the commercial banking system or the companies that any of the weaker banks should participate in such financing, and this will particularly apply to the numerous banks formed in recent years in this country. This new class of business requires much experience and an established policy of sound banking. It also demands considerable capital and a firm resistance to the speculative temptation which easily arises in a line of business where securities are created and sold. The bulk of the joint stock banks in India are at present not ready for this activity, and even the larger ones can cultivate it slowly, with great caution and preferably under competent guidance.

2. It is desirable that a commercial bank, which has business relations with industrial companies should have somebody on its management, say, an assistant manager, who is fully conversant with the financial side of industries in general, so that its operations with industrial concerns may be facilitated.

3. There is need for a sympathetic attitude on the part of banks towards industrial companies. This was the secret of the German banking policy in respect of her industries. German banks used to delegate a member of their management to act on the Board of Supervisors of companies with which they had business relations in order to maintain a close connection with those companies. The presence of these bank delegates was of considerable use to the industrial companies in view of their general experience in finance. It was also of advantage to the banks themselves as a measure of protection against losses. In fact the system of close intercourse between banks and industrial companies thus brought about created an atmosphere of mutual confidence with resultant benefit to both parties. With the object of creating a sympathetic attitude on the part of banks towards industrial companies, it is useful to have banks' local advisory committees in important trading centres. A number of joint stock banks have got at present such local advisory committees. Such local boards are very useful and desirable not only to help the bank in assessing the financial position of its clients, but also in removing from the minds of its clients the suspicion of unfair or unsympathetic treatment. In order not to weaken the responsibility of the management it is, however, necessary that these local boards should be invested with functions of a purely advisory character.

4. Banks in India insist on the full backing of liquid assets for their loans and take no account of valuable block capital. While the question of deciding about the nature and adequacy of securities offered for loans should be left to the final decision of the banks themselves, there is obvious need for a more liberal policy on the part of banks in this respect. Industrial compa-

nice in India may reasonably expect to have the whole of their working capital supplied by commercial banks, if adequate security to the satisfaction of the banks is offered and if it is recognised by the borrowing companies that the banks can demand repayment of the whole or part of the amount lent, if necessary.

5. Banks in India lend much less on personal security than in other countries. The grant of advances on personal credit in Western countries is, however, limited to big firms of undisputed standing. It is not possible to recommend an indiscriminate extension of the system of granting clean credits by banks in India; but with the increase in the number of similar large firms the reluctance of banks to lend without security should gradually diminish. If banks make no difference between borrowers of different standing and follow the same policy in all cases, there should be a change of policy on their part both in the interests of the borrowers and the interests of the good name of the banks, otherwise the banking methods would be stigmatised as primitive.

German Banks and Industry. The following is a brief description of the relations between banks and industrial companies in Germany as they existed before the World War II.

An industrial company in Germany had what was called a current account connection with its bank, which was distinct from the current account as used in relation to banks and their clients in England or in India. In the ordinary current account connection, the customer was sometimes in debt to the bank and sometimes had a balance to its credit. Many claims thus arose on both sides which were not settled individually but were settled periodically, usually every six months. The extent of the industrial company's indebtedness, the maximum period for which it might be outstanding, and the security to be given were fixed by agreement from time to time after consideration of all the circumstances of the case. The current account advances were used by the average German company not only for the purpose of providing itself with working capital but also for supplying block for extensions in anticipation of recourse to the investment market.

The industrial companies in Germany provided themselves with initial capital in two ways. Either the promoters invited the public to subscribe the capital and to help to bring the company into existence; or the promoters themselves took over the entire capital in the first instance with the intention of placing the shares among the public subsequently. Although promotion of industrial companies by subscription was the general practice at an early period of German industrial development, the second method is said to have completely ousted the first in later years. In connection with the second method of promotion, because the investing public either required a lead or felt a reluctance to decide on participation in an undertaking before it was fully launched, banks in Germany had played an important part in providing

the greater part of the initial capital, which was subsequently placed among the investing public. In order to reduce the risk borne by a single bank and to ensure the success of the issue, it was very common for several banks to join together in what was called a *consortium* and pledge themselves to accept a certain portion of the issue. It is important to notice that the investment of German banks in shares of industrial companies was not a long-term investment and was resorted to merely as a safe and liquid investment for part of the bank's resources in first-class securities. It is not inconceivable that circumstances might arise when on account of the issue proving unsuccessful, the banks might be compelled to hold the securities almost indefinitely. But such a situation can be regarded as involuntary and incidental. From the bank's point of view, its participation in the promotion of new industrial companies was considered useful for acquiring business connections or extending the bank's influence.

It would thus be seen that, when an industrial company wished to procure new capital, whether from existing shareholders or by issue of new shares or debentures in the general capital market, it arranged the transaction with the bank with which it was in permanent banking relations. The ordinary banking business in which deposits from the general public are employed is decidedly the most important business of German banks. In addition there is a department for industrial and similar finance, with a limited share of the bank's own resources, for carrying on financial transactions arising from time to time in the relations of the bank with the industrial and similar joint stock companies. These financial transactions require a certain amount of capital investment which is kept in conservative relation to the share capital and reserves of the bank. While it remains more or less stable in the aggregate, its composition is changing as quickly as market conditions allow. If the public is not responsive to the offer of securities resulting from such industrial financing, it follows that the banks cannot continue their assistance to industries until the public is again prepared to put up the new capital required.

The Industrial Finance Corporation of India

The need of a well-organised agency for industrial finance in India has been seriously felt for a long time. A great deal of interest has been focussed on the question of industrial finance in recent years in view of the fact that India is now on the threshold of large-scale industrial development. The Industrial Commission appointed in 1918 gave great prominence to this question of financial facilities for Indian industries in their report and stressed for the first time the desirability of establishing special institutions for financing them. The Banking Enquiry Committee of 1929 also emphasised that India had a great industrial future and it was highly desirable that steps should immediately be taken for providing short, medium and long term financial assistance to industries. But nothing came out of these recommendations.

The subject of industrial finance has assumed great importance since the

cessation of hostilities in 1945. In most of the industrially advanced countries, various types of institutions have been set up for the purpose of providing long term finance to industry. In Britain two finance corporations, viz., the Finance Corporation for Industry Ltd., and the Industrial Finance Corporation Ltd., have been started for financing small and large industries. In Australia the Commonwealth Bank has created an Industrial finance department, and in Canada the Bank of Canada has set up a subsidiary company known as the Industrial Development Bank of Canada for supplying adequate credit to industrial enterprises. At last our national government has also fulfilled this long felt demand by enacting an Act to establish the Industrial Finance Corporation of India.

The management of this Corporation is entrusted to a Board of Directors which with the assistance of an Executive Committee and a Managing Director will exercise all powers and do all acts which may be exercised or done by the Corporation. The Board is to act on sound business principles having due regard to the interest of industry, commerce and the general public. The general policy is to be decided by Government, and if the Board fails to carry out the instructions on the question of policy, the Government will have the power to supersede the Board and appoint a new Board in its place to function until a properly constituted Board is set up. The Corporation's Board of Directors will consist of twelve persons of whom three will be nominated by the Central Government, two by the Reserve Bank of India, two will be elected by the scheduled banks, two by the co-operative banks and two by the other financial institutions. One Managing Director is to be appointed by Central Government. The Managing Director will be a whole-time officer of the Corporation and perform such duties as the board may entrust or delegate to him. He will hold office for four years and be eligible for reappointment and receive such salary and allowances as the Board with the approval of the Central Government may determine. The chairman of the Board will be one of the directors (not being the managing director) and be nominated by the Central Government. He will hold office for two years or until his successor is nominated. The Executive Committee will consist of two directors elected by the nominated directors and two directors elected by the elected directors and the Managing Director who will be the chairman of the committee. The Corporation will establish its head office in Delhi and offices in Bombay, Calcutta, Kanpur and Madras. It may also open offices at other centres with previous sanction of the Central Government.

The main object of this Corporation is to make medium and long term finance more readily available to industrial concerns particularly in circumstances where normal banking accommodation is inappropriate or recourse to capital issue methods is impracticable. It will not supplant the commercial banks but supplement them by providing long term capital. Some of the more important functions which the Corporation has been authorised to perform are as follows:—

1. Guaranteeing, on such terms and conditions as may be agreed upon, loans raised by industrial concerns which are repayable within a period not exceeding 25 years and are floated in the public market.
2. Underwriting the issue of stock, shares, bonds or debentures by industrial concerns.
3. Receiving in consideration of the above services such commission as may be agreed upon.
4. Retaining as part of its assets any stock, shares, bonds or debentures which it may have to take up in fulfilment of its underwriting liabilities and then disposing of these as early as practicable and in any case within a period of seven years from the date of such acquisition.
5. Granting loans or advances to, or subscribing to debentures of, industrial concerns repayable within a period not exceeding 25 years.
6. Generally doing all such matters and things as may be incidental to or consequential upon the exercise of its powers or the discharge of its duties.

It should be noted that the Corporation will provide financial assistance to public limited industrial concerns or industrial co-operatives. It means that private limited companies and partnership firms cannot have the benefit of services of the corporation. It has also been laid down in the Act that no financial accommodation will be given unless it is secured by a sufficient pledge, mortgage or assignment of Government or other securities or other tangible assets. The maximum amount of accommodation given by the corporation to a single industrial concern will be limited to ten per cent of the paid-up capital of the Corporation but in no case exceeding 50 lakhs of rupees. A notable feature of the Corporation is that it can make loans to the companies in need of finance either in Indian currency or in any foreign currency if it is thought appropriate. For this purpose the Corporation is authorised to borrow through the International Bank for Reconstruction and Development. Although the Corporation is not expected to provide financial help to Government-owned industries yet it has been permitted to take up government loans and to invest its funds in the securities of the Central Government or any Provincial Government.

The authorised capital of the corporation is Rs. 10 crores divided into 20,000 shares of Rs. 5,000 each, of which 10,000 shares will be issued in the first instance and the remaining shares will be issued from time to time as and when it is deemed fit. The Central Government and the Reserve Bank of India will each take up 2,000 shares. Each of two groups (that is, the scheduled banks and the other financial institutions such as insurance companies, investments trusts, etc.) will be allowed to subscribe each for 2,500 shares. The remaining 1,000 shares will be offered to co-operative banks. It has also been provided that no institution will be allotted more than ten per cent. of the shares reserved for the class to which it belongs. If shares

offered to those different institution remain unallotted they will be taken up by the Central Government and the Reserve Bank of India in an agreed proportion. These shares are not transferable except to those different types of subscribers.

Besides the share capital, the corporation will derive finance by way of deposits and issue of bonds and debentures. The total of all borrowings, together with contingent liabilities of the corporation, should not exceed five times the amount of the paid-up capital and the reserves fund of the corporation. The deposits accepted by the corporation from the public are to be long-term ones and the total amount of such deposits will not at any time exceed ten crores of rupees.

The repayment of share capital and the payment of the annual dividend at such minimum rate as may be fixed by Government are guaranteed by the Central Government. After making provision for bad and doubtful debts, depreciation and all other matters which are usually provided for by banks, the Corporation may declare dividend out of its net profits. The maximum dividend payable is 5 per cent. per annum but this level may not be reached until a reserve fund equal to the paid-up capital has been created and all the sums paid by Government under guarantee are repaid by the Corporation. If in any financial year, the reserve fund becomes equal to the share capital and if there is after declaring a stipulated dividend, any surplus, such surplus, will be paid to the Central Government. It has been also laid down in the Act that the Corporation should pay income-tax and super-tax, as if it were a company under the Indian Companies Act. But any sum paid by the Central Government under guarantee is not liable to income-tax and hence any dividend paid out of any such sum, will also be treated as tax-free.

The Corporation has been given wide powers to prescribe the necessary conditions for the borrowers. These include the right of the corporation to appoint its nominee on the Board of Directors of the borrowing companies.

If any industrial concern makes any default in repayment or fails to comply the terms of its agreement the Corporation will have a right to take over the management of the concern as well as the right to sale and realisation of the property pledged or assigned to the corporation. It has also been given powers to call for the repayment of any loan or advance before the agreed period by giving a notice if the industrial concern has given false or misleading information in the application for the loan or failed to comply with the terms of the contract with the corporation or become unable to pay its debts or commenced proceedings for liquidation or ignored to insure property pledged or removed the pledged property without replacing it.

The Central Government have been given sweeping powers by the Act in regard to the control and management of the Corporation. Thus, it is the Government that has to lay down the broad principles to be followed by the Board in discharging the functions and the Board has to be guided by the Central Government on questions of policy; and in the case of a dispute as to

whether any question is or is not a question of policy, the Central Government's decision is to be final. The Central Government has also been given powers to supersede the Board if the latter fails to carry out the principles of policy as laid down by it. Further the number of directors is so fixed as to maintain an even balance between Government and other shareholders. The Government will have the power to demand a classification of its loans investments and of loans guaranteed by it and underwriting agreements entered into at least once in every year and also a statement in the prescribed form of its assets and liabilities as at the close of each year together with a Profit and Loss Account for the year and report of the working of the corporation during the year. The Government has been also given power to acquire shares held by shareholders after paying an amount equal to the paid-up value of shares together with a premium calculated at the rate of one per cent. of the paid-up value for every year from the date of issue to the date of acquisition subject to a maximum of ten per cent.

(d) Managing Agents and Company Finance.

The managing agency system is the foundation of the existing methods of company finance in this country. India does not possess the industrial banking system of the Continent, nor are there any issue houses, investment bankers and the underwriting firms of the Western type. Their place in company finance is taken in India by the managing agency system. The provision of finance not only for initial fixed capital expenditure but also for subsequent reorganisation, extensions and modernisation as well as for working capital purposes has to be arranged for by the managing agents, and they furnish this finance in the following ways :—

1. They themselves subscribe to the share capital and debentures of joint-stock companies and also get them subscribed by their friends and relatives. A cursory look at the company prospectuses that have appeared in the press during the last few years will show the extent to which the managing agents and their friends and relatives have taken up the shares and debentures of companies in India.

2. They act as a link between the company and the bank when a bank loan is arranged on their guarantee. When granting short-term loans to companies, banks in India almost invariably insist on the guarantee of their managing agents.

3. Many companies in India obtain a large part of their permanent capital by means of public deposits, which are attracted only on the good name of the managing agents.

4. They are expected to render financial assistance to the companies under their control in times of emergency. For the purpose of financing schemes of extension and reorganisation managing agents have frequently furnished long-term loans; and during the development period or during a period of depression when banks would not advance money or the public would not take

up debentures, they have rendered considerable financial assistance to the companies under their management. There are numerous instances where the managing agents have saved companies from complete ruin by giving timely loans.

5. By affixing their name to the prospectus of a company, the managing agents induce the investing public to come forward with their money for subscribing to the shares and debentures of the company. The well-conducted and reputable firms of managing agents created confidence in the minds of the investing public.

6. In recent years the managing agents have also acted as underwriters by underwriting the shares and debentures of the companies under their management.

The managing agency system has rendered a very valuable service to Indian companies by furnishing the necessary finances directly or indirectly; but this system of financing by managing agents has not been free from certain defects which are as follows:—

1. The practice of investing the surplus funds of one company in the shares and debentures of another company under the same managing agents is perhaps the greatest evil. Under this system of inter-company investment a sound company may suffer for the sins of the unsound. Fortunately this practice is now completely prohibited by section 87-F of the Indian Companies Act.

2. Where a firm of managing agents has a number of companies under its management, its resources may not be adequate to render sufficient financial assistance to all the companies. In recent years there has been a tendency on the part of many agency firms to add to the number of companies under their control.

3. Banks in India grant credit to companies on the strength of their managing agents and not on their own financial stability. Therefore if the financial position of the managing agency firm becomes weak, the banks withdraw their credit from the companies.

4. In view of the fact that companies depend to a large extent on the financial facilities extended by their managing agents, industry in India is too much dominated by financial considerations and too little by industrial factors. Finance instead of being a servant of industry becomes its master with injurious results. Industrial capacity is thus subordinated to finance. It means that a firm which commands substantial financial resources very often acquires the managing agency of a company, although such firm does not possess any industrial or business talent.

The cost of finance supplied by managing agents to the companies under their management is usually high, and in some cases managing agents charge exorbitant rates of interest for their loans.

6. Where financial assistance from the managing agents is readily forthcoming, it is quite possible that the company's own internal resources in

the shape of reserves may not be strengthened, thus keeping the company constantly dependent upon the managing agents.

7. Some of the methods adopted by managing agents in financing companies have been found to be highly objectionable. In a number of cases the managing agents have turned their loans into debentures with the result that the concerns have passed into their hands and the shareholders have lost all their capital invested in them.

8. Owing to the birth of many new companies, there has been a deterioration in the quality of managing agents. The old and well-established managing agency firms have no doubt rendered invaluable financial services to companies; but the new managing agents cannot all be expected to possess all the characteristics of the old agency houses.

On the whole, it may be stated that the financial services rendered by the managing agents are most important in the earlier stages of the career of an industrial company and ought to become less and less as the company is firmly established except in periods of depression. In a country where banking development has been very slow, where difficulties of raising permanent capital from investors are great in the initial stages of an enterprise, and where at any rate during the period of the inevitable handicaps to the growth of a new company some financial assistance of a kind, which the commercial banks cannot render, is necessary, it is obvious that the managing agents can fulfil a very useful function.

(c) Public Deposits

One of the peculiar features of Indian company finance is the use of public deposits for financing not only current needs but in some cases also the extensions. This system is very common in Ahmedabad. It also obtains to some extent in Bombay and is not unknown in other parts of the country. In its origin the system of deposits with industrial concerns was undoubtedly a reflex and a transformation of the old system of keeping money for safe custody with the mahajan. In Bombay and Ahmedabad the men who founded the mill companies were either merchants or shroffs in whom the public had confidence, and hence their savings were entrusted to them.

Ahmedabad has developed the system of seven-year deposits, and all the new companies there have been financed on the basis of long-term deposits. Such deposits are, therefore, the nearest approach to debentures, and from the point of view of companies they are better than debentures, because the depositors have no lien on the assets of the companies. Although serving the purpose of debentures, such deposits rank *pari passu* with short-term deposits. The inducement to such long-term deposits is very often the right to a share in managing agency commission, but for which these would not have been attracted. A fairly large part of the financial requirements of a new company in Ahmedabad is met by these long-term deposits, and these funds are utilised for block expenditure.

The rates of interest payable on deposits vary with the credit and stability of the companies and their managing agents. If the managing agents of a company are men of standing and reputation, large amounts of public deposits can be attracted on very favourable terms to the company. Even where the deposits are for short periods, say six to twelve months, they are generally renewed.

The advantages and disadvantages of this system of finance may be stated to be as follows :—

Advantages 1. It enables a company (by keeping its capital low and by borrowing at cheap rates) to pay higher dividends than would be possible if the whole of its long-term finance were in the form of share capital.

2. Where the public deposits are for longer periods, they serve the purpose of debentures without any charge being given on the assets of the company in favour of depositors.

3. The cost and formality of issuing either shares or debentures are avoided. The receipt of deposits and their repayment are quite a simple affair.

4. The capital plan of a company, which uses this system of finance, remains elastic. As its property is kept free from charge, it is always in a position to raise further finance, if necessary, by issuing debentures. If on the other hand, it finds itself overcapitalised, it can simply refuse to receive further deposits or to renew the existing ones when they mature.

Disadvantages. 1. The short-term deposits are liable to be withdrawn in times of depression and adversity as actually happened during the depression of 1925-26. They are after a 'fair weather friend'. When they are withdrawn in a period of panic, the company will hardly have any other alternative source of finance.

2. There may be a temptation of overtrading which easily secured loans usually encourage. With money obtained at relatively low rates companies may be prone to speculation and may be tempted to carry larger stocks than would be justified by market conditions.

3. When short-term deposits are locked up in fixed capital expenditure, a company may not be in a position to repay them on the due dates with consequent damage to its credit and reputation.

4. The losses, which must occur in a crisis or panic owing to short-term deposits being locked up in fixed assets, would tend to frighten away many people both from investing in industrial shares and from putting their money on deposit with banks.

5. The system of public deposits with industrial companies restricts the supply of good industrial securities available for the ordinary investor and unduly narrows the market for such investment.

Although some companies have come to grief on account of financing by means of public deposits, yet there are in existence many companies which

have derived immense benefit from this system. The success of any system of finance depends largely upon the quality of a company's management. Financing by public deposits may not be an orthodox method, but it would hardly be fair or reasonable to condemn it when it has successfully stood the test of time for about half a century.

Test Questions

1. Examine in detail the part played by hundis in the sphere of business finance in this country. *(Agra B. Com. 1946)*
2. Describe briefly the financial needs of modern industries. How do industries in India usually obtain their working capital? *(Agra B. Com. 1945)*
3. What points would you bear in mind when devising the capital structure of a proposed public limited company? *(Agra B. Com. 1944)*
4. Discuss the important part played by financial houses in underwriting and otherwise financing joint-stock companies. *(Bombay B. Com. 1935)*
5. Distinguish clearly between a preference share and a debenture from the point of view of the company and the investor. Is the debenture always safer? *(Bombay B. Com. 1945)*
6. Why do joint stock companies raise their capital by different kinds of shares? *(Bombay B. Com. 1944)*
7. Point out the distinguishing features of the different types of shares issued by a joint stock company. *(Rajputana B. Com. 1949)*
8. Most joint-stock companies raise the funds they require by means of ordinary share capital, of preference share capital and of debenture stock. Do you regard this threefold division as due to economic causes, or is it merely conventional? *(Bombay B. Com. 1934)*
9. Discuss the relative merits and demerits of deposits, bank loan and debentures as methods of business finance. *(Bombay B. Com. 1937)*
10. Why should a Joint Stock Public Company issue different classes of shares? Name the different classes of shares issued and discuss the rights of each class with regard to (1) Dividend, (2) Capital, and (3) Voting. *(Bombay B. Com. 1938)*
11. A Limited Company requires more capital for financing increasing business. Point out the advantages and disadvantages for the issue of shares and debentures. *(Bombay B. Com. 1939)*
12. Explain clearly what you understand by a Non-cumulative preference Share and a Participating Preference Share. Give reasons why a large part of the capital raised by industrial concerns in India is accounted for by Preference Shares than by debentures. *(Bombay B. Com. 1940)*
13. How is the cotton mill industry of India financed? *(Agra B. Com. 1947)*
14. Discuss the different methods of industrial finance in India, and show why debenture issues are irregular in this country. *(Agra B. Com. 1948)*

15. (a) What are the different methods by which joint-stock companies are financed in India ?

(b) What part do managing agents play in Indian industrial finance ?

(Allahabad B. Com. 1940)

16. Discuss in detail the part which the system of public deposits has played in the sphere of industrial finance in India. (Agra B. Com. 1945)

17. An existing mill company with a good dividend record wishes to raise a further capital of Rs. 10 Lakhs for financing a projected extension scheme. Its present authorised and issued capital consists of 25,000 shares of Rs. 100 each, fully paid, all shares being of the same class ; and it has not issued any debentures

Examine briefly the various methods available for raising the additional finance, and state with reasons which method in your opinion would be the best in the circumstances mentioned above. (Agra B. Com 1944)

18. Distinguish between the several legal forms under which working capital is obtained for joint stock undertakings

19. What is the role played by Indian banks in financing business concerns ? What improvements would you suggest ?

(Rajputana B. Com 1949)

CHAPTER 9

MODERN METHODS OF PUBLICITY

The object of all business is to make profits and a merchandising concern can do that by increasing sales at remunerative prices. Advertising and salesmanship are both sales aids—means to attain a given end.

1. Advertising

'Advertise' not till the last century meant 'to inform' or 'to take notice of.'

There has been a gradual transition and the word today has acquired purely a commercial significance. Advertising today signifies something modern, something which has arisen only within the last few generations. Advertising in the modern commercial sense is the investment of money for the purpose of disseminating information and ideas, usually with the purpose of selling something. It is used thus for the purpose of making commodities known to as wide a public as possible; to arouse interest in them, to establish confidence in them, to influence the mind of the buying public, and to create and stimulate demand.

The only way to find a permanent and ready market for anything, whatever it may be, is an intelligent and regular advertising. No amount of honesty, reputation or commercial travelling unassisted by advertising can exhaust the possibilities of demand. Advertising can make the goodness of good goods known to the millions, and, in most cases, it can do this far more quickly and far more profitably and effectively than if each pleased customer were simply left to tell its merits to his friends. Advertising can change the whole aspect of a branch of trade. It can force the tradesman to stock the products which he hates. It can multiply human wants. It can educate people to know the essential qualities to be looked for in products of this or that kind. It can transfer trade from one article to another, from one shop to another, from one street to another, from one town to another, and from one country to another. It can alter the habits of the people. It can alter fashions in dress, in eating, drinking, smoking and reading.

Economics of Advertising. From the economic standpoint, advertising is undoubtedly of great significance—a significance which manifests itself beyond the frontiers of the home country into the sphere of world economy. Large numbers of people subsist on advertising and its associated activities. It gives employment to a very large number of people—artists and writers—and an employment too in which ideas count and in which originality is stirred. It is a good training for young businessmen, especially where there are opportunities for progress and improvement. The news and periodical press is subsidised to

such an extent by the heavy prices obtained for space that it is almost certain the public can buy daily, weekly and monthly literature at half the price it otherwise would have to pay.

Large groups of consumers, and sometimes even the whole nation, is influenced in their requirements by advertisements. They are introduced to new wants, the wants are strengthened or cast aside and new ones take their place. Indeed, the advertising of such concerns as big retail stores, apart from the goods they sell, seems to have filled a household want. What a blank there would be in the lives of the uncountable ladies if all these advertisements were completely withdrawn from the daily, weekly, and from the fashion and illustrated papers.

Advertising is a great educative force. It spreads information about manufactured goods far and wide. It is a great labour-saving device. It makes an attempt to eliminate the middleman. It is a good substitute for travelling salesmen. It is the essence of economy in producing, in selling and distributing goods. It increases the employment in the country, stabilises the prices of commodities and improves the standard of living of people. Most of the new inventions would not have been business propositions without advertising.

Advertising introduces new contrivances, promotes variety in production and consumption, often it is a means of useful competition. Effective advertising is a gain to the producer, it is a gain to the consumer, if greater utility and satisfaction result from the substitution of one article for another. Advertising can inculcate new virtues of thrift and prudence. The advertising of life assurance has taught people their responsibility to their dependents, and has saved many from penury. Lastly it is a source of goodwill. It is now beyond dispute that many of the most important businesses have developed and created their goodwill by means of advertising.

Advertising, like other things, is not an unmixed blessing, and it has got a darker side too. Some of the objections raised are :—

1. All advertising means expense and this must be paid by somebody. The claim of advertising to reduce cost is not true in all cases. Therefore in some cases this adds to the cost to the consumer.

2. The sovereignty of the consumer is destroyed. The consumer purchases not what he wants or likes but what he has been influenced to buy. He is not the final judge of his needs and the means to satisfy them. It is the advertiser who determines what the customer shall purchase.

3. It leads to waste and extravagance. The consumer is allured by attractive advertisements and is tempted to purchase luxuries rather than necessities.

4. Advertising brings about rapid changes in styles and fashions, and these sudden and frequent changes mean loss to the consumer as well as to the retailer. The retailer has to sell at a loss goods which have gone out of fashion.

5. Advertising is generally associated with adulteration of food and substitution of worthless goods for articles of proved quality. This becomes possible because the consumer is led to believe the high sounding statements made in advertisements, and he cannot distinguish between genuine and fraudulent goods.

6. It is almost inseparably bound up with exaggeration, misrepresentation and falsehood. Cheap medicines sold by quacks endanger the health and morals of the young and the innocent.

It is difficult to say as to who bears ultimately the burden of the expense of advertising. It is even more difficult to say with any exactitude what part of the cost is borne by the advertiser or the consumer. The purpose of advertising is to reduce to the minimum the expense of selling goods. Any saving in selling expenses may either increase the manufacturer's profit or reduce the price to the consumer. Owing, however, to competition consumers largely benefit from it. That 'advertising reduces cost' should be taken with caution and should be accepted only as a half-truth. The arguments justifying the claim have application to a certain number of trades and to certain methods and that also to a limited extent. If the article happens to be of wide use, advertising may lead to mass production, thus reducing the cost of manufacture and distribution. In such cases the price to the consumer may be reduced, the profits to the producer may be increased, and the cost of advertising is borne by advertising itself. In other cases the cost of advertising is a cost of salesmanship and is paid by the ultimate buyer.

Advertising is the most powerful weapon in the hands of the modern trader, but it is a weapon with a terrific recoil and frequently liable to explode at the breach. It has achieved amazing successes, hurrying some struggling firms from obscurity into front positions and creating goodwill values of staggering worth. It is not, however, a casual affair. It does not grow out of the untutored inner consciousness of the advertiser; nor does it descend from heaven on a desert of the undeserving. It is an annex to business; its principal outer courtyard has to be studied in the interests of business. All business grows ultimately from honesty, intensity and efficiency of advertising. That is the writing on the wall of every prosperous business.

There are certain things which advertising can do and others which it cannot do. It is not a conjuror's wand, which can bring white rabbits out of a silk hat or fortune out of folly. It cannot in the long run sell goods for less than cost and make a profit on them. It cannot make a permanent success of a bad article. It cannot bring anything but financial ruin on the fool who offers sawdust to the public for breakfast food. It cannot ensure success to a product in spite of mismanagement in its manufacture or wastefulness in its distribution. It cannot produce perpetual motion, commercially speaking, by creating a demand that will continue undiminished without further effort. It cannot force people to keep on asking for a thing which cannot be obtained,

It cannot change the customs of people in a day or two. It cannot achieve success in defiance of the laws of economics and psychology.

In short, advertising has a number of limitations, but still the art of advertising is one that pays its devotees, bringing success to those who are faithful and make the fewest mistakes, and despite all its disappointments, it is the real driving force of every business that has made itself great. The possibilities of advertising in business, nationally and internationally, are so enormous that we can scarcely grasp them.

Organisation of Advertising. The first difficulty facing a sales manager, when preparing for an advertising campaign, is to decide the amount which ought to be set aside for the purpose. The average business man does not go into details and very frequently the amount is fixed arbitrarily. In large businesses, however, various estimates are prepared, problems facing the undertaking are considered, the objective to be achieved is decided, and the appropriation is then determined by consideration of all these factors.

Before actually embarking upon an advertising campaign, it is highly desirable that a suitable advertising plan should be framed. It ought to be decided whether advertising is at all necessary, and this can be indicated by looking into the activities of competitors and the information gathered through market research. It should also be considered whether adequate stocks are available to meet the increased demand as a result of advertising. It is always well to set an objective, a standard, and then to take steps to achieve it.

A point arises whether advertising work shall be entrusted to an advertising agency or be undertaken by the advertising department of the undertaking itself. It depends upon the circumstances of each case, and unless the amounts involved are large and the finances of the undertaking strong, it is generally better to entrust the work to an advertising agency who shall do the work cheaper and better.

The advertising department is an important adjunct to the selling organisation of any concern. The department is generally placed under the charge of an Advertising Manager who is a responsible and experienced advertiser and salesman himself and who is given a decent remuneration. He must be able not only to plan advertisements but also to see that he gets the largest possible benefit from the quota allotted to him by way of advertising expenditure by the management.

The advertising department, although a separate unit under an independent person, should not be an end in itself. The object of the advertising department is to increase sales with a view to increasing the profits, and therefore the advertising department should be subordinate to the general sales manager. The policies of the advertising manager should be discussed, determined and laid down in collaboration with the sales manager. It is the sales department which only knows what is to be sold and what is the problem of selling which is to be solved by advertising. The advertising manager should consult the

sales manager and should devise his advertising plan to fit in with the object of the sales manager. The function of the advertising department is to make the work of salesman simpler and easier. Salesmen should be kept informed of the current advertising plans of the business, and the advertising department should constantly send the salesmen the necessary advertising literature and instructions to facilitate their task of creating the demand and persuading the customer.

Further the advertising department should always run in consonance with the general policy of the undertaking. It is the advertising department that should be adjusted to the changing needs of the business and not the business to the needs of the advertising department. Advertising has to be modified by the financial policy of the concern. It is in accordance with the financial aspect that advertising media, type of advertising, the copy, the space, the frequency of appearance in the media, etc., will be determined. If large funds are available, advertising can be planned from a long-period point of view, and the best media can be employed to get the best result.

The modern advertising agency is a group of specialists who undertake to look after every class of advertisements and also arrange the direction of advertising campaigns. Each specialist has a wide knowledge of his particular sphere of activity. The knowledge of this group is placed at the disposal of clients retaining the services of the agency. They render service both to those who are unable to maintain a special advertising department as well as to those who can afford this luxury. To the former they act as special advertising departments; advise them as to the design and get-up of advertisements, prepare advertising material such as copies, circulars, book-lets and other literature; design wrappers and packages for their wares; suggest appropriate media for publicity; plan marketing procedure; and finally arrange for purchase of space at favourable rates. These agencies undertake the distribution of literature, fixing of placards and posters in proper positions and looking after their safety, and so on. There are some obvious advantages of advertising agencies. The advertiser is relieved of much detailed work and is left free to concentrate on sales, marketing and production. By reason of the gross amount of space purchased for its clients, the agency commands a certain amount of goodwill, and clients are enabled to secure spaces at favourable rates and to obtain better positions than they could otherwise do. It is thus that a small trader is able to secure the services of experts whose employment as full-time workers would be well nigh impossible even for much larger concerns. The agency has experience at its command about the most effective media and the way how they can be used. This is placed at the disposal of the clients, and often some of these services are rendered free to the clients, because agencies in many cases are remunerated by publishers, who themselves stand to gain from advertising agencies a great deal.

Advertising by Wholesalers and Retailers. The method and form of

advertising is different for different businesses. The method and type of advertising has to be selected in accordance with the nature of a business and its peculiar requirements. Advertising is a means to achieve a given end and therefore advertising has got to be adjusted to the special requirements of a business. A wholesaler has entirely different conditions in his business from those which obtain in the business of a retailer. The goods dealt with, the nature of the prospective customers, the expense involved, are all different in the two kinds of businesses.

The fundamental difference between the advertising of a retailer and that of a wholesaler is that the retailer aims at attracting people into his shop to satisfy the requirements, whereas the wholesaler merely creates the demand for his goods and is not particular as to where that demand is satisfied,—so long it is satisfied. Wholesalers' advertising is mainly directed to "the trade." His activities are so extensive that for his business he has to rely on advertisements in his trade journals and on direct mail advertising by the issue of circulars, catalogues and price lists. The campaign of the retailer, on the other hand, is usually a local one restricted to those media with a circulation in areas whose inhabitants can conveniently visit him for their shopping requirements.

As regards the advertising policy of the wholesaler, he advertises on a national scale and an appeal is made to a very large number of people spread throughout the country. The retailer, on the other hand, seeks to attract specific type of individuals as his main customers. The retailer seeks to create an atmosphere of exclusiveness and individuality. He tries to have some 'speciality' about his business—quality, character of the product, design, style, or any other point.

The media of the wholesaler are of the widest and general circulation. The aim of the wholesaler is to bring the goods to the notice of the largest number of people, and for that he advertises in the papers of extensive circulation, in trade journals reaching a particular section of the community, fixes the trade names of certain proprietary goods and makes use of other media if necessary. The advertising of the retailer is necessarily local, unless he has some mail order business also. The medium most commonly used by retailers is the local press. National media represent a sort of wasted circulation, and so is the case with boardings except in the immediate vicinity of the shop. Signs in trams, buses and other means of conveyance proceeding along the route to the shop may be of value, especially in large towns. Advertising in local cinemas may be used with greater effect in the case of big retailers. Canvassing may sometimes be used. The retailers repeat their advertisements at regular intervals, sometimes announcing seasonal goods.

Generally speaking, the situation may be summarised by saying that the wholesaler by his national advertising aims at stimulating consumer demand for his product in a general way. When the wholesaler has created this

demand, the retailer must capitalize upon it, featuring the goods advertised in his own shop and so supplementing the national advertising.

Cooperative or Group Advertisements. Advertising may be competitive or cooperative. In competitive advertising, an individual trader or firm advertises his or its own goods, whereas in group or cooperative advertising several manufacturers or traders dealing in a particular line of goods combine together and advertise together for all the members. This may be done to encourage the use of particular commodity or to educate the public. Indian Insurance Companies' Association advertises on behalf of its members, in order to encourage insurance with Indian companies. It may be undertaken to prevent the people from buying foreign goods.

Technique of Advertising

Advertising Campaign. By campaign is meant the whole selling effort for a season or other period of time during which a special drive is made to secure the desired result. This purpose should be written down and expressed in exact language and should not be unattainable; commonsense and experience should show that it is a possibility. The purpose of an advertising campaign is as follows.

1. To determine the market—its size, the nature of people—their class, time of purchase—regular or seasonal, the mode of purchase—in bulk or small quantities.
2. To decide the channels of distribution—are the existing ones satisfactory or is it necessary to introduce some innovation or modification?
3. To determine the scope of the campaign— which parts of the country are to be reached?
4. To determine the advertising media best suited to the purpose which shall be least costly.
5. To discover the basic and central idea on which the advertising appeal is to be based. On the strength of the appeal will depend the effectiveness of advertising.
6. To decide the fundamental human desires to which the advertising will appeal.
7. To decide the tone of advertising—argumentative, suggestive, educational, etc.
8. To determine the amount of space that shall be bought and the position of the advertisement.
9. To prepare the advertising copy to place the copy with the publishers and to supervise the conduct of the campaign.

Advertising Media. The advertising costs money; and, unless rightly directed, most of the money spent on it can be wasted; therefore, the media for an advertisement campaign should be selected by certain principles, not because they are recommended by some friend nor because a competitor uses them. Some idea of the relative effectiveness of various media may be gained

material through the post and destroy it without reading it, they may visit picture houses but pay no attention to advertising films or slides, or they may possess wireless sets and never listen in to stations broadcasting advertising.

Some periodicals are regarded more highly than others by the public and the tendency is for this regard to be passed on to the advertising carried by these periodicals. The claims of advertisements appearing in periodicals with a high reputation are more likely to be believed than those appearing in periodicals of a lower order.

A factor of considerable importance in assessing media values is their life. The daily newspaper is read in a few hours at most, and then probably cast aside. In contrast magazines when read by one person are passed on to others. They may have a life extending over long periods. The "life" of a poster is again different. A man passes in a few minutes but one may pass the poster every day for a long period. The life of a leaflet can only be as long as a person stops to read it, perhaps a fraction of a second or several minutes. If the medium is a utility such as a catalogue, a directory, a blotter, and inkstand, or a calendar, then by reason of its utility its life may be very long, and also valuable because of the fact that it is being continually seen and used.

(a) Press Advertising

The press is the most extensively used advertising medium for all general purposes. The chief reasons for this are two—firstly newspapers or magazines of some kind are read by the largest number of persons daily, and secondly advertisements in the press can be of any form according to the requirements of the advertiser. Here there are more opportunities for selection.

Press advertisements may be divided into two classes—classified and unclassified. 'Classified' advertisements are usually brief statements giving particulars, names, addresses, descriptions, details of value and sometimes prices. They don't readily attract the eye, but they serve the purpose of a handy reference when a person is interested in any of the goods or services mentioned. For unclassified advertisements there is relatively unlimited space, i. e., a page, a part of it, or several ones.

The press advertising media are daily and weekly newspapers, magazines and specialised journals. Each one of these media may be used for a country-wide campaign; but the purposes for which they may be used differ. The national dailies may be used with advantage, but if it is desired to strengthen the campaign in areas not adequately covered by the national dailies, other provincial papers may be used. The evening papers provide an opportunity for local advertising. The function of the weeklies and magazines is different from that of the dailies, since their life is longer and they tend to pass through more hands. These represent the method of steady and regular building of business and not to effect quick impressions. Specialised media such as sporting publications, children's papers, etc., have a very clearly defined appeal, their circulation being limited to certain groups or types of individuals,

A press advertisement to be effective must have wide appeal, it must satisfy a general rather than an individual need. This appeal is the most important part of the advertisement, because it is this appeal which determines the action of the reader to buy or leave the commodity advertised. The appeal must be one in which the majority of people, whom it is hoped to influence to buy the product, will be interested. To be read, the advertisement must be like the news in well-edited paper—of such a nature and so presented that it will not be read either by accident or because people have nothing else to do, but because the information it contains is of pertinence to some satisfaction of their needs or else in itself it is interesting. It need not be counterpart of sensational 'news-scoop'. A story should be built about the product.

The appeal should be adjusted to the particular desires of the customer. For this it is necessary to study the customers, their desires, habits and needs. Account should also be taken of competitors' appeal. It pays to profit by the mistakes of competitors. Once the customers have been carefully studied, the appeal may be directed to one or more of their desires and instincts such as (1) Self-preservation instinct—need for food, warmth, health and efficiency, freedom from disease; (2) Parental instinct—protection for children, ministering to their needs and happiness; (3) Social desires—self-assertion, ambition, ceremonial and conventional activities. In order to choose the strongest appeal for a particular commodity, the commodity itself may be considered. For example, in cheap motor cars, economy would be a good appeal, while in high-priced cars, comfort and social distinction would be better. In the case of a soap for the dhobi, constituents and cleansing qualities would be appropriate, while for that for personal use, appeal to beauty and pleasantness in use and disinfectant properties would be effective.

Copy-writing. The copy writing is perhaps the most difficult piece of work with which a man is faced in connection with advertising. The work is generally entrusted to an artist who knows his job and who alone can do it in the most satisfactory manner and to the best advantage. There are certain fundamentals which must always be embodied in a good advertising copy. The aim of the advertising copy is that it shall be seen, read, the message conveyed and then acted upon. In other words the three fundamental points are attracting the attention, holding the attention and appeal and response. These may be considered briefly as follows:

(a) *Attracting the attention:* The observing power of the majority of people is weak, and therefore it is assumed that people will not see a thing unless their attention is drawn to it. The attention of the people is drawn readily and more quickly by novelty. For example, nobody cares for a bus while many look at the aeroplane. It implies that in order to attract attention the advertisement should have something of novelty or of unusual association. People are too busy these days, and unless their attention is particularly attracted, they are likely to ignore the advertisement. For this purpose various

colour combinations together with suitable pictures or illustrations can be used with great advantage. Position of the advertisement also is an important consideration. If it occupies a central position with regard to other competing advertisements, it has better chances to attract attention. This is the main reason why full page advertisements in magazines and newspapers carry the greatest attention value.

(b) *Holding the attention.* An effective advertisement must hold the attention long enough to make a lasting impression by creating an interest in the subject of the advertisement with little or no conscious effort. This is done by bringing into the mind an easy association of ideas. This may also be done by wide-spread and continuous intermittent advertising. Repetition helps people to remember. The repetition of a trite phrase, inclusion of trade name or trade mark in every advertisement is intended to impress that phrase on the mind. Repetition, however, defeats its own object unless presented with variety.

Other methods to improve the attention value of the advertisement are pictures, use of display types, use of colours, borders, use of reply coupons, attractive headlines and slogans, leaving space either at the head or foot of the advertisement, etc.

(c) *Evoing the response.* An advertisement should be an appeal to human thought and feeling. That is, it should attract the attention and create interest in the goods advertised. For this the advertisement should include a suggestion for action in some form or another. It may be the action of memory, deduction of reasoning, or the action resulting from an emotion aroused or belief established. The advertisement should therefore have conviction and sentiment value as well.

Some other requisites of a good copy are as follows :—

1. Copy must be expressed in concrete terms. Definite examples must be given to carry conviction. Vague generalizations, however brilliant, are useless.

2. The concrete ideas conveyed in this way must readily link up with the ideas already existing in the reader's mind, i. e., they should be in continuity with his needs, his dispositions at the moment, or else they should have some reference to current topics of specific news interest.

3. The copy must be appropriate to the product, to the types of individual who may be expected to read the advertisement, the time of year when the advertisement appears and the class of media employed. If the product is sports equipment, the copy must be sporting; if it is something dignified the language should be developed accordingly. If the appeal is to children the language must be simple.

4. The copy should say that it is desired to say in as few words as possible. This does not mean that any item of importance to the final effect of the appeal should be omitted. If the message is expressed labouriously and not

concisely, it is less likely to be read, less likely to be understood, and less likely to be remembered. In addition, conciseness means that less space need be bought for effective presentation.

5. The copy must be easily understood. The message must be so expressed that the immediate interest of the reader is obtained and its implications readily grasped.

6. The method of writing must carry conviction. The copywriter must be convinced of the genuineness of his appeal and argument before he can hope to be able to convince the reader.

7. The copy must aim at creating desire and showing the best means by which this desire can be satisfied. It must essentially suggest action. In other words, the copy in the final analysis must be such that it influences people to buy the goods advertised.

8. To help arrest attention, the design or layout of the advertisement should be striking or different.

9. The headline should attract attention, tell the story and arouse interest. Unless his interest is awakened the reader flicks the pages till his sophisticated eye rests on something that promises not to bore.

10. The copy should not be 'clever.' It should be fresh and piquant. The reader must be led to think not of the words written, but of their message. The claims made in an advertisement should be moderate and of a nature to inspire belief.

11. Illustrations are a great help, and are used for one or more of four purposes in an advertisement: to gain attention, to make ideas more vivid, to create an atmosphere, and to get action.

12. The selling point should be appropriate.

The one thing that really counts always is that the copy should create the right impression and that impression should not be dulled by a multitude of words and details. The copy should also be individual to the thing advertised. It should concentrate on a main feature associated with the article.

A copy not conforming to the above-mentioned principles is a copy which shall defeat its object. It might have been prepared with great labour and expense, but, unless it serves its purpose, it is a waste. A large amount of money is simply thrown away by careless advertisers through the neglect of these principles.

The object of advertising is generally to make people to buy, not merely to think or talk about certain wares. Most of us are probably perfectly familiar with the names of the patent medicines we have never taken, pianos we have never touched, boots we have never worn, books we have never read, cigarettes we have never smoked, cocoa we have never drunk, dramas we have never seen, soaps we have never used, whisky we have never tasted, summer resorts we have never visited. Advertising has utterly failed here.

We may mention below some of the weaknesses of the copy in the form

of doubts which must be avoided in all cases :—Don't be vague or make false statements or generalisations. Don't be verbose or use excessive formal or difficult language and unnecessary long words. Don't give opinions, but present facts when the purpose is to convince the customer. Don't use superlatives and negative statements. Don't lie or exaggerate. Don't place out of place questions or phrases, which will irritate the customer.

The "Lay-out" of the copy may be defined as the arrangement of the matter including illustration or picture or block of a trade mark, if any, in the copy of the advertisement for the guidance of the compositor. Its object is to give the compositor a rough picture of what the advertiser wants his advertisement to be, in the form in which he would like it to be set up in types and block. The width and depth of the advertisement should be stated. In short, all that the layout claims to do is to prepare and place before the printer a typographical diagram guiding him as to the form in which the advertiser wants the matter to be composed and built up, and indicating the place where display as well as picture has to be shown. All instructions to the printers should be given in the margin with a ring round them.

When it is desired to assess the relative values of different media or to compare the pulling power of individual advertisements and media, the advertisements are generally keyed, e. g., by directing the reader in one advertisement to address to Department A, and in another to address to Department B. Keying devices like the following are in use :—

- (1) Write for our folder on "How to Know a Good Watch."—it's free.
- (2) A Book of Beautiful Cars" will be sent you on request.
- (3) Ask for Booklet No. K-23.
- (4) Coupons to be cut from advertisements.
- (5) Name the magazine when replying.

Press advertising offers certain advantages. An appeal can be made to a selected class of readers. It enables the business to sell through the post. It provides for both direct and indirect selling. It affords opportunities for lengthy appeal, because the people who are reading publications are obviously in the mood of reading or looking at pictures. It serves as an introduction to follow-up system. It gives ready means of distributing folders, coupons or application forms.

(b) Mural Advertising

Mural advertising (or better out-door publicity) is one of the several forms of advertising, and it always functions as being 'suggestive' and reminder rather than argumentative advertising. The object of this kind of advertisement is generally to create an atmosphere about the product, to keep its name and possibly one or two of its outstanding features before the public, or also to indicate where a product may be obtained.

Mural advertising is most frequently used to supplement press advertising. It is unsuitable for many specialised products, which are not to be of interest to

the necessary effect, and they carry an instantaneous message. Where, however, the picture is not used, the words of the advertisement should be concise; it must be 'telling' enough to be read quickly and to be remembered. For that a high degree of legibility of the distance is very necessary, to ensure which the trade name of the article may be emphasised by putting it in large print and by backing it by a 'slogan'. The 'slogan' is a phrase which appeals to the mind because it is an apt and trite saying. "Press the button and we do the rest", "the King of Soaps—the Soap of Kings" are two of the examples. Something may be provided also to ensure a powerful suggestion to action with perhaps some indication where the product may be obtained. The following are the principal forms of mural advertising:—

Posters. The term poster is used here to include advertising messages printed on paper, cardboard, wood, or metal, and either exposed to view on hoardings, railway stations, on the sides of roadways, or attached to the internal or external walls of shops, etc. Previously poster advertising was rather in disrepute; the situation has changed today. Elaborate hoardings have been designed to harmonise with their surroundings, many of them with beautiful landscape gardens in front of them. The poster itself has developed from the unpleasant circus-bill type to the delicately coloured, well-printed creations of artists, whose fees for designing the poster are commensurate with the creative genius necessary. They should be of standard size, so that they can be interchanged. Special attention should be bestowed on their printing and it should be ensured that the posters will be in harmony and continuity with the other aspects of the campaign.

Posters offer some important advantages and one of them is that advertising can be localised and concentrated in any town, market or street. Moreover, they are a very suitable form of advertisement for commodities which are needed by people when out of doors or on the street. They serve to remind people about things which have been known by them or previously brought to their notice, but which they are likely to forget. To get the best results, a site completely isolated from other posters, corresponding to the 'solus' position in the newspaper, should be selected.

Where the posters are exposed to weather, and it is likely that they will be damaged as a result, the design may be painted by hand or unadorned signs may be used. But this method does not readily lend itself to frequent change and adjustment to changing needs and conditions of the business. They are expensive also. At times, however, they can produce striking artistic effects.

Posters may be illuminated by flood lights or other means so that they can be seen by day as well as at night. If people are likely to be passing the poster during the night, it can be made to carry the advertising message by night as well as in the day. Arrangements should be made for the light to be automatically turned off during the hours when people will not be passing the site. It is also important that the lighting should be so arranged that the original colours

and effects are not lost in any way.

Electric Displays. Signs illuminated by electricity are used extensively in the more crowded cities of the world. The appeal of the light, colour, and movement which they make forces itself very vividly upon the attention. Electric signs are usually arranged on roofs or on walls. There can thus be no standard size. Copy for use in an electric sign must be brief and may be limited to the name of the product or organisation and a slogan, or at most a few words. Some electric signs are operated on the motograph or change system, by which a series of advertisements can be shown from one sign or several different messages can be shown in sequence. The electric sign depends for its effect on the brightness of its illumination and the brilliance of its colours. Thus several colours in a sign are more effective than a single one, and coloured sign is more effective than one using white light only. Unless extremely large numbers of people are going to pass by the sign to and be influenced by the electric sign, the heavy expenditure involved is not justified, and probably the money should be spent with better effect in other ways. They can be very expensive and unproductive luxury if not used with discretion.

Bus, Train and Tram Advertising. Cards and posters may be displayed in buses, buses and trams, and the spaces secured in this way may be the outside spaces which differ only from ordinary poster sites by reason of the fact that the buses and trams are moving. The inside space on buses and trams, etc., differs from ordinary poster site in that people are forced to sit and look at the advertisements for much longer periods. This is a great advantage. The traveller is not in a hurry and so long as he remains in the vehicle, his attention is constantly directed to the display which is so arranged that it be constantly before the eyes of the traveller. On the other hand, the copy need not be very brief and more facts and information can be usefully supplied. The advantage of this form of advertisement is further increased in case of local buses, trams and trains where practically the same travellers travel from day to day excepting for a few persons who might be casual visitors to the town or who come only occasionally.

Sandwich-Board Advertising. Sandwich boards are a method of localized advertising and are of some use in drawing attention to services and facilities offered by shops, theatres etc., adjacent to where the sandwich men parade, but which otherwise may not have public attention drawn to them. Further the use of the sandwich boards as a medium is gradually falling into disuse, perhaps because it is a means of achieving through tedious and poorly paid labour an end that can be attained equally well by other methods. Sandwich-men are usually hired by the day at so much per man from a contractor who supplies the men and the boards and supervises their activities according to the advertiser's instructions as to where he wants them to parade.

Mural advertising has the following advantages: It makes a wide appeal to all classes of people. It is effective in getting public interest and opinion

of the same problem. Advertising influences the customer at a distance and is about a general want ; whereas salesmanship is an adjustment to a particular want and, as the prospect is before the salesman, it administers to the individual need rather than the general. Salesmanship is the basis of all commerce, the first and last object of which is to market goods and services to the mutual profit and lasting satisfaction of the buyer and seller. It is a service essential to the producer and distributor of goods as well as to the customer.

There are some misconceptions existing in the minds of people regarding the work of salesman, and unfortunately the salesman's profession is not regarded in our country with the respect and dignity it deserves. He is not a door-to-door "hawker", as the term often seems to have been understood by the public. He belongs to a noble profession and he is one who has cultivated an art which has its root in the natural aptitude and peculiar capacity for it. Salesmanship, on the other hand, is not the mechanical process of handing over goods to a customer. Machines are now doing this work, but they do not do the work of a salesman.

We may now consider the services which a salesman renders to the society. The object of all activities is the satisfaction of wants, and all production is undertaken for the same purpose. The ultimate object of the manufacturer and distributor is to sell their goods at a profit. Sales are the life blood of a business, and dwindling sales its chief killing disease. Salesmanship is the touchstone of all business ; the salesman is the backbone of industry. He helps the producer and the distributor to distribute their goods for the mutual benefit of the buyer and seller. He helps the producer and consumer to get more closely in touch with each other. It enables the producer to adapt himself to the particular needs of the consumer. The salesman gives information to the producer about the particular requirements of the customer, and the producer and the distributor are enabled to work together to satisfy those requirements. He makes exchange easier ; he opens new markets ; he overcomes obstacles to trade ; he brings necessities and luxuries to large multitudes.

Personal Qualities of a Salesman : A successful salesman must possess some inborn attributes and personal qualities. They are cheerful disposition, ambition, aptitude, resourcefulness and enthusiasm, patience and tact and good taste. In addition, the salesman should possess good health and freedom from physical defect. Persons with seriously defective vision or impaired speech must be ruled out.

A cheerful disposition. The gloomy and sour type of person does not make good sales. It is the brightly cheerful salesman who smiles his way into the customer's favour and who is able successfully to lead on the customer from purchases to purchases.

✓ Ambition. Ambition is essential in any person intended for a course of training of any description. The desire for promotion and progress is the chief

motive power and guiding force. If the desire is absent, nothing can happen.

Aptitude. Possession of a natural aptitude for selling is a valuable asset. To a person having this aptitude, salesmanship will be a source of never-failing fascination. Any industrial psychologist will tell you that uncongenial work is far more exhausting to the individual than that which is congenial. The young apprentice whose heart and soul is in selling does not watch the clock and pray for closing time to come. He has fallen under the spell or perhaps the most fascinating game in business selling. He is intensely interested in the little human dramas being played out around him. He is absorbed in the study of that most engrossing thing human nature.

Resourcefulness and enthusiasm. Resourcefulness is properly regarded as an inborn aptitude, whereas enthusiasm may come by cultivation. The person, who realises the importance of the work entrusted to him, must display energy and enthusiasm in order to properly do his job. Enthusiasm is catching and the sales person who can naturally and spontaneously work up enthusiasm is at least halfway to success.

Patience and tact. Tact is the adjustment of one's relationship with others. In other words, it means understanding other person's point of view and giving him satisfaction. It is a necessary requisite for the equipment of the successful salesman so that the customer may not be offended by an awkward remark. The best tact is often the outspoken and forthright candour that addresses the duke or the dustman in precisely the same way. A toady, ing and wheedling accent rarely pleases anybody, least of all the person who has money to spend. Patience is another quality and it is very necessary in trying circumstances. In the presence of some difficult customers, it becomes difficult for the salesman to maintain his balance. It is the patience which helps him.

Politeness and good taste. The salesman must be polite and courteous to the customer and must show good taste. Good taste is valuable when the salesman is called upon to advise or assist the customer in making his choice.

Other requisites of a successful salesman are thorough knowledge of the goods sold, and a sympathetic and hopeful attitude.

Principles of Salesmanship. There are the same four fundamental principles, as in advertising, on which the salesman has to work, viz., attracting the attention, arousing desire, convincing the prospect, and impelling him to action.

Attracting the attention. Attracting people into the shop is necessary because a salesman's work begins when the customer is inside. The important thing is to attract the passer-by and to lure him inside. The shop sign and the number of the door must be distinctive, attractive and lasting. It should give some idea of cleanliness and smartness. There should be proper arrangement for lighting. Have a door and entrance which is wide enough to admit of easy access. Make your shop an easy shop to enter. Entrance should be

advertised in the press or otherwise, this service becomes all the more important because advertisement attracts, it does not sell. It is the job of the salesman to interest the customer and sell to him. The object of advertising is to keep up a steady stream of visitors, it produces sales opportunities. It is then up to the sales staff to exploit these opportunities. It is folly to spend large sums on advertising to attract customers in large numbers, if nothing is done to ensure that the potential purchasing power of those customers will be exploited to the full when they arrive at the store. Indifferent salesmanship can turn the advertising expenditure into a dead loss. The interest aroused by advertising is only a frail and delicate growth, and it requires nursing. It is only the tentative opening of a sale. The customer who has positively made up his mind to purchase on the strength of the advertisement is one in a hundred. The other ninety-nine are no more than mildly interested and require encouraging, not discouraging. The following points may be noted in this connection.

Stock must be handy, convenient of access, easily distinguishable by its position and labels and capable of being produced quickly for the customer's inspection. Articles of common use and for which there is frequent demand should be nearest to hand and others should be within easy reach. It gives good impression if the article asked for is produced quickly with smartness and precision.

Cleanliness is always a paying proposition, dirt and damp must be avoided because they only repel the customer. Proper temperature should be maintained, extremes being avoided and the comfort of the customer should be given due consideration. In summer the fan may be switched on for the customer without distinction, while in winter arrangements may be made to save the customers from exposure.

The goods should be shown in suitable groups, numbers or quantity to increase their effectiveness and to permit an easy choice. They should be shown and so displayed so as to bring out their strong selling points and so as to suggest, through the eyes, their best position in use.

Customers should be attended to in order of their arrival. If not, people may resent it, though some may bear it with good grace. The salesman should have quick perception, good memory and a sense of justice.

It is a mistake to disparage the goods of another make, but the salesman may properly point out the particular ways in which his own article is superior. If the customer gets the idea that the salesman is unfair even in little matters, he may consider the salesman untrustworthy and refuse to buy.

4. *Impelling to action or closing the sale*.—No two men 'close' in exactly the same way. Most men, however, are influenced by the suggestion that the offer now made may be withdrawn at any time. If the trend of the market is upward, this may be used as an incentive for immediate action. An appeal to

pride or the desire to be exclusive may be used to advantage with a certain type of customer. He may be told that the goods in question are much in demand and that they may be soon sold out while there is no immediate or early prospect of fresh arrivals. Above all things, do not make yourself obnoxious if you cannot make the sale; remember that you may want to sell this same man something next week, next month or next year.

Here are a few don'ts for a salesman. Don't appear too hasty in your conversation. It takes time to convince a man and close the sale. Don't mispronounce your customer's name. Don't allow yourself to become angry over any irritating things he may say. Don't spend all your time in explaining the mechanism of your article to a man who is interested only in what the thing will do:

Though the customer may not always be right, it is invariably a good policy to let him appear to be in the right. Give the customer the benefit of doubt, and do not be too ready to classify him as difficult. The great majority of customers are pleasant, decent people who will respond to sympathetic treatment. The customer is a guest of the firm—and a welcome paying guest. Thank the customer who comes back to make a sincere complaint. That gives you the opportunity of putting right something that may be wrong. Do not try to show the pompous customer that you are "as good as he is". You may be, but he is the customer, and that makes all the difference. Learn how to take shelter tactfully behind "the rule of the house," when dealing with a customer who expects favoured treatment.

Test Questions

1. "It pays to advertise". Do you agree? Justify your view by specific reasons. *(Rajputana B. Com. 1919)*

2. "Money spent on advertising is wasteful." Do you agree? Give reasons for your answer. *(Bombay B. Com. 1947)*

3. What channels are available to a manufacturer to market his products? Which method would you advise a manufacturer of fountain pens to adopt and why? *(Bombay B. Com. 1916)*

4. Examine carefully the principles of effective advertising and suggest methods by which an advertisement may be made to appeal effectively to an illiterate public. *(Bombay B. Com. 1943)*

5. Outline briefly the organisation and describe the working of the advertising department of a large firm. What methods are available for testing the effectiveness of its advertising? *(Bombay B. Com. 1912)*

6. By what principles would you be guided to selecting the medium for an advertisement? Bring out the relative merits and demerits of news-papers and magazines as advertising media. *(Bombay B. Com. 1912)*

7. What points should the advertisement of a life insurance office bring out in order to induce the public to become its policy holders?

(Bombay B. Com. 1911)

8. Discuss the principal elements which should be present in a good copy of advertisement to appeal to :

(a) an urban community,

(b) a rural community.

(Bombay B. Com. 1934)

9. What are the chief characteristics of a good copy of newspaper advertisement ?

Discuss the possibilities of (a) railway trains, (b) Theatrical programmes and (c) shop windows as advertising media.

(Bombay B. Com. 1934)

10. Messrs. Allum & Co. are manufacturers of high class leather suit cases in Bombay. Draw up an advertisement for them not exceeding five lines and mention the media you would utilise.

(Bombay B. Com. 1936)

11. Review the merits and demerits of the different media of advertising.

(Bombay B. Com. 1947)

12. State the various methods by which the display value of an advertisement in (1) a newspaper and (2) a magazine is improved and draw up a layout as well as a copy of an advertisement for a magazine in connection with a maker of a radio set in the sale of which you are interested.

(Bombay B. Com. 1937)

13. State what elements a scientifically drafted copy of an advertisement must embrace ? Draft a copy of an advertisement of a patent branded breakfast food for children embracing appeal to the appropriate instincts.

(Bombay B. Com. 1937)

14. How would you explain to an advertiser who has never used posters, their suitability for this proposition, detailing the object with which the posters are to be used as helps to other forms of advertisements.

Draw up a poster which you would recommend in the above case.

(Bombay B. Com. 1938)

15. Modern advertisement has made the luxuries of yesterday the necessities of to-day. Comment on this statement, giving suitable examples in support of your answer.

(Allahabad B. Com. 1938)

16. Write a short essay on 'Mural Advertising'.

(Agra B. Com. 1944)

17. State briefly the essentials of a good newspaper advertisement, and draw up a suitable advertisement (for insertion in a financial weekly) on behalf of a life insurance company or a bank.

(Agra B. Com. 1945)

18. A glass manufacturing company has been recently started under good auspices. How should it, in your opinion, arrange for the publicity of its products ?

(Agra B. Com. 1946)

19. Enumerate the Principal characteristics of a successful salesman and discuss if engagement of a saleswoman would in this country, augment the sales of—

(a) a departmental Store,

(b) a retail Store.

(Bombay B. Com. 1934)

20. What are the requisites of good salesmanship and efficient advertising ? Draft a specimen advertisement for the foreign press on behalf of a Benaras silk house.

(Agra B. Com. 1947)

CHAPTER 10

INSURANCE

Risk is an element which is quite common, though not certain, with men and things. In order to eliminate the undesirable effects of this uncertain element and to provide against any unexpected contingency, the need for insurance arises. It is encouraging that in India people are fast realising the splendid opportunities and increasing facilities afforded by insurance, which, though not in the nature of preventive of risks, saves one from losses. In the words of Sir Mirza Ismail "Insurance is like the quality of mercy. It blesseth him that gives and him that takes. Insurance cures for you from the cradle to the grave."

Insurance is a contract by which one person undertakes to indemnify another person against a loss which may arise or to pay to him a sum of money on the happening of a certain event. The basic principle of insurance is that the individual's risk is spread out and shared by the community, the medium of such social cooperation being the insurance company. Insurance is therefore a cooperative device. It brings together a number of individuals who may be exposed to a similar risk in order that they may assume it collectively. The risk, which would otherwise be borne by only an individual, is distributed over a large number of persons.

The person who agrees to indemnify or to pay a lump sum is called the "insurer" or "assurer", while the person who is to get the indemnity or the sum of money is known as the "insured" or "assured". The consideration for the contract is a single or a periodical payment called the "premium". The document containing the terms of the contract of insurance is called the "policy" which requires a revenue stamp. There are many forms of insurance available at the present time, and it is now possible to insure against almost any risk to which man is exposed. Insurance may, however, be divided into two main classes—Life insurance and non-life insurance. The latter term also known as general insurance includes fire insurance, marine insurance, motor car insurance, third party insurance, workmen's compensation insurance, insurance against riot and civil commotion and so on.

Assurance and Insurance. Though these two terms are often treated as interchangeable, yet the former should be applied only to life risks which are certain to happen. Insurance, on the other hand, refers to those risks which are contingent in their nature, as fire, marine, accident, etc. Therefore insurance relates to events which may partly happen or partly fail; assurance is dependent on the duration of life.

Essentials of Insurance Contracts. A contract of insurance, like other contracts, is governed by the Indian Contract Act. In order that it may be valid it must possess the same essentials as any other contract does, namely, there must be offer and acceptance, competent parties, genuine object and consideration. Contracts of fire and marine insurance are *contracts of indemnity*, that is to say, compensation is payable to the person insured only for the loss he has actually suffered. A contract of life insurance, on the other hand, is not a contract of indemnity, but it is an absolute undertaking to pay a specified sum of money in a certain event.

An insurance contract must possess two additional features. The first of these is that the assured has an insurable interest in the subject-matter of insurance, that is, he must be in such a position that he will benefit by the safety of the subject-matter insured, and sustain a pecuniary loss in the event of its being lost or damaged. What persons are supposed to have an insurable interest will be explained later. It may, however, be pointed out that in life insurance the interest must exist at the time the policy is completed, in marine insurance it must exist at the time the loss takes place, whilst in fire insurance it must exist both at the time the insurance contract is completed as well as when the loss takes place. In the absence of an insurable interest the insurance is merely a gambling or wagering agreement, which is void at law.

The second feature of all contracts of insurance is that they are said to be contracts *uberrimae fidei*, i. e., contracts requiring a disclosure of all material facts and the observance of utmost good faith. According to law misrepresentation renders an ordinary contract voidable at the option of the party deceived. In contracts of insurance, however, something more is required than an absence of misrepresentation. The insured must disclose every material fact within his knowledge which would be likely to affect the judgment of the insurer. If any information which is within the knowledge of the insured is withheld from the insurer at the time of entering into the contract the policy would be void. This obligation is imposed by law owing to the fact that the insurer has no access to information which is in possession of the insured.

Doctrine of Subrogation. This applies only to contracts of indemnity—fire and marine insurance. Where the insurer has paid for a total or for a partial loss, he thereby becomes entitled to the benefit of all the rights and remedies of the insured in respect of the subject-matter so paid for. The transference of these rights and properties to the insurer is known as the doctrine of subrogation, e. g.—

(a) A insures his house with B. The house is destroyed by fire set to it by a neighbour C. A recovers the damage from B. Here B is entitled to A's right of suing C for damages.

(b) An insured ship is reported as missing and the insurer pays for a total loss. Should the ship be subsequently found, it will become the property of the insurer.

This right of subrogation can be exercised by the insurer only on payment of the loss sustained by the insured. Further the insurer can enforce only those rights which the insured himself could have enforced, and he must sue in the name of the insured.

Double Insurance This means effecting more than one insurance on the same adventure or interest. In life assurance two or more policies may be taken out on the same life, and the amount of all the policies can be legally recovered from the insurers. But in fire and marine insurance this is not possible, as they are contracts of indemnity only. If there is double insurance in respect of the same subject-matter, and the sum insured exceeds the indemnity allowed by law, the insured may claim payment from the insurers in such order as he thinks fit, but he must give credit for any sum received by him under any other policy. Should he receive any sum in excess of the indemnity allowed by law, he is deemed to hold it in trust for the insurers according to their rights of contribution among themselves. As between the several insurers each is liable to contribute his proportionate part ratably, and any insurer who pays more than his proportion of the loss is entitled to contribution from the other insurers.

For example, suppose that property worth Rs. 12,000 is insured against fire with three companies, namely, with X for Rs. 4,000, with Y for Rs. 5,000, and with Z for Rs. 6,000 in all. If the house is totally destroyed by fire the insured can claim only Rs. 12,000, the value of the property and not Rs. 15,000, because a fire policy is a contract of indemnity where only the amount of actual loss can be claimed. This loss of Rs. 12,000 the insured can claim from any of the insurance companies in whatever way he likes but not exceeding from each the amount for which the property was insured. Thus he may claim Rs. 6,000 from Z, Rs. 5,000 from Y, and Rs. 1,000 from X. But the loss of Rs. 12,000 will be borne by the three insurers proportionately, i. e., in the proportion of $4/15$ $5/15$ and $6/15$ respectively, and any company which pays more than the amount of its share of loss is entitled to recover from other companies which have paid less than their due shares.

Reinsurance. An insurer, who has accepted a risk greater than he thinks prudent for himself to retain, can reinsure the whole or a part of it with another insurer. This is called reinsurance and is usually subject to the same law as that which governs the original insurance. The reinsurance policy contains a declaration that it is a reinsurance contract. Reinsurance is possible in all forms of insurance—life, fire, marine, etc. Reinsurance must be clearly distinguished from double insurance. Reinsurance implies the insuring of a risk or a part thereof already undertaken by one insurer with another insurer. Thus a contract of reinsurance is entered into between two insurance companies and the insured has nothing to do with it and his position remains unaffected.

Life Assurance

Life assurance is a form of insurance by which the insurer undertakes, in

consideration of a single or periodical premium, to pay the person for whose benefit the assurance is effected, a specified sum of money on the death of the person whose life is insured or on his attaining a certain age.

With the individualistic tendency of social organisation life assurance is growing in magnitude every day. More and more insurance companies are formed and an army of agents is recruited by every concern to meet the growing competition. The advantages of life assurance cannot be denied except by spiritualists who condemn such a provision as arising out of lack of faith in God. But for a worldly man it is necessary to make provision for his old age and for those who are dependent on him. There are numerous cases where respectable families have to lead miserable lives after the death of their earning members. The joint family system is an alternative against this contingency, but it is breaking asunder, and people are becoming more and more individualistic.

There are two elements present in life assurance—the element of protection and the element of investment. The former is present in all other kinds of insurance as well such as fire, marine, accident, etc., but the latter is found only in life assurance. It is the element of investment that makes the premium on life assurance so high and that gives surrender value to a policy of life assurance. When a person deposits money in the Post Office, there is only an element of investment. The money goes on accumulating at compound interest until it is withdrawn by the depositor. In the event of the depositor's death the Post Office will not pay more than what has been deposited plus interest due thereon, because there is no element of protection in a Post Office account. On the other hand, there is fire insurance in which there is only an element of protection but no element of investment. If a person insures his building against fire for a year and there is no loss by fire in that period, he cannot take back anything from the insurance company on account of the premium he has paid. The insurance company only guarantees that in case of loss by fire it shall solemnly insure, but if there is no loss there can be no claim, as there is no element of investment in a fire policy. But both the elements of protection and investment are found in a life assurance policy.

Need for Life Assurance. Most people nowadays recognise the need for life assurance and every year the world grows more and more insurance-minded. Ever since the Wall Street crash in 1929 and the subsequent depression, when literally thousands the world over lost much of their wealth, people of both affluent and moderate means have come to regard life assurance with a fresh interest and for the simple reason of stability and safety. During those dark days, one investment, which did not depreciate in value but which paid a full measure of sixteen annas in the rupee in strict accordance with its terms, was the life assurance policy.

But human nature being what it is, we all desire to get rich quickly. We risk hard-earned money hoping that by some conjury it will flow back into our pockets several times greater. When the share market rises and we make a little

money we are jubilant, but we never stop to inquire why the market rose; it is only when we lose money on its fall that we start wondering. There is no magic road to wealth. Steady, persistent and regular saving is the surest and most certain method of accumulating wealth. Statistics disclose that ninety-five out of a hundred men reaching the age of 65 have little or no money. Of the ninety-five, twelve are physically able for a time to go on working for a living, while the remaining eighty-three will be dependent on charity.

What is adequate assurance is an individual matter not only as to the amount but also as to its wise application, and the major controlling factor is the length of our purse strings. Let us suppose a person is now aged 27 his wife 25, and he has one child, a boy aged one. He is not a merchant prince, so he will have to budget his salary extra carefully. Ten years hence he will most probably be seriously considering the education of his boy, but in addition he will have a far more satisfactory income. Twenty years hence his genial smile and expensive cigar will indicate the success of his business. But these anticipations and their realisation are joined together by the fragile and slender thread of his life. So let us be practical and take first things first.

As a young man with little or no accumulation of money, he requires as much protection for his family as his purse will allow. If he is thinking of taking a little insurance now and a little later on, he may not get that further amount later, because he cannot guarantee the state of his future health. For an annual premium saving of approximately 4 per cent. of the sum assured, an ordinary life policy would provide maximum protection. Again, supposing his salary cheque has stopped, not for just a month or two, but for ever, his wife has still to carry on. What is the minimum income on which she and her child can live? It will be found that almost all insurance companies will pay out proceeds of a policy in quarterly, half-yearly or annual instalments.

Having arranged this primary essential—(the ideal of course being to guarantee the independence of his widow for life) the consideration of having funds for the education of his children comes next. Whether or not he takes out any insurance for the purpose, he will have to educate them. So, later, when he can afford to save additional money, a short term educational endowment or, if this falls too heavily on his purse, a further ordinary life policy to give the necessary protection in the event of his death, whilst making his own savings as he may be able, should be the next step in his programme. If he is sufficiently well protected, he may convert it to an endowment for his own retirement benefit.

At this stage he is probably 40 years of age and has no longer so great a need for the protection of his family. His income in the normal course of events should be decidedly greater than what it was fifteen years ago, and he will now be viewing the future with much clearer vision than the dim horizon he visualised as youth. Now let us consider his own retirement plan. If he cannot afford to convert his life policies into endowments, he should carry them

on. At retirement their surrender values and bonuses will help to purchase an annuity which will yield an income in excess of their annual premiums, the later his retirement the greater the annuity. What surplus he can afford to save may be invested in endowment assurances maturing at his probable retirement age.

Life assurance is a dire necessity A ship may sink, a building may burn, but every man must die. The beauty of life assurance is that it reaches its maximum value when everything else is made uncertain by death. The man who procrastinates may be sorry that he met ill-health before the insurance agent overtook him. If a person cannot accumulate a capital, he can create one by investing in life assurance. Will a man's earnings continue after his death? Yes, if he insures them. By means of life assurance one can continue one's income after retirement—or for the benefit of his dependents after his death. In case of death, the bank pays what one has saved but the insurance company pays what one hoped to save.

Objections Against Life Assurance. The man who objects to assure his life 'on principle' is not so frequently met with nowadays as formerly, doubtless owing to the nature of the subject being better understood. Still, insurance agents are sometimes exasperated by coming in contact with a man who, for some reason, does not believe in life assurance and remains impervious to all the arguments usually comprised in the agent's repertory; and it may be of service to field-workers and others to consider some of the objections and prejudices that occasionally require to be overcome.

There was a time when a great many people looked askance at life assurance on religious grounds and even today the fact that a concern depends for successful development on the remunerative investment of its accumulated premiums at interest handicaps agents who strive to do business among very orthodox Mohammedans and those who hold the view that the employment of money to yield interest must always be tainted with usury. But even pious Hindus and Christians who are free from the exaggerated idea of usury have been known to argue that to assume one's life indicates a want of faith and that the care of one's wife and children in case of premature death can be safely left in the hands of Providence. This comfortable way of looking at the matter does not take sufficient account of the fact that Providence generally works through some human agency. If death occurs, the necessary assistance to the sufferers must come from others who survive, which exactly corresponds with the basic principle of life assurance that those who live long compensate the financial loss involved by those who die young. "Bear ye one another's burdens" might well be chosen for the motto of a life assurance institution, which reduces mutual protection to the form of a business-like system. A man, who has the means of availing himself of this system and does not do so, and has made no other provision for his family, is following a line of conduct that suggests presumption rather than faith.

Of much more frequent occurrence is the objection that life offices hoard up enormous funds derived from premium contributions, that such vast resources are unnecessary, and that the contributors have paid far more than actual requirements, and that except in the event of early death (which these objectors always regard as a most unlikely contingency) the man who effects a policy will probably pay dearly for it in the end. In short, it is implied that the public are exploited, and more often than not weight is lent to this contention by examples being quoted of cases where an assured, desirous of closing his contract, has been offered a surrender value of much smaller amount than the premiums he has paid. The increasing funds of life offices should be no more a matter for adverse criticism than growth of total bank deposits from year to year. Depositors in course of time withdraw their money, and similarly policyholders either die or their policies mature and the amounts due are paid out of the general fund; the larger the number of new policyholders, the greater will be the natural increase in the funds. The periodical valuations of life offices show the amount which must be kept in hand and invested to enable a company to meet all existing liabilities as they fall due (taking account of future premiums expected to be paid under the policies (valued) and the surplus is returned to policyholders in the form of bonus additions to their policies.

Then there is the man who thinks he can do better with his money. If he can, it is generally on account of having special opportunities not open to the average man. The amount he would otherwise pay in premiums may perhaps help in this business to a small extent, or bring in a handsome return at some future time if he lives to receive it. But in any case he would be running a risk at the expense of his dependents. In the great majority of cases, life assurance is not merely the best way a man can make immediate provision for those who would stand to lose by his death; it is, generally speaking, the only way. It provides a capital sum that is free from the chance of depreciation, and if the company is selected with ordinary prudence it is as safe a means of investment as any other channel to be found anywhere. It is significant that successful business men are generally the first to appreciate the advantages of life assurance and never raise any objections to it.

Here are a few more objections against life assurance together with their answers. "I am not interested in insurance." Not interested in your wife and children's comfort! Your wife and children might have to suffer the hardships of poverty if you do not now interest yourself in safeguarding against this by insuring yourself. "It may not be possible for me to continue paying premiums to keep policy in force." Life is so uncertain. Who knows you may have only one premium to pay? Then again, just consider if you cannot manage to pay premiums on your insurance which is the most effective way of creating an estate for your dependents, in what way are you going to provide for their future when they are left alone to face the necessities of life without even your income? "My income is not sufficient and I will consider

when I have better income." Suppose your income were reduced by Rs. 15 or Rs. 20 a month, would you not manage your expenses to suit your reduced income? Since you can adjust yourself to your reduced income, it naturally follows that you could save this much from your monthly income towards ensuring the future welfare of those near and dear to you. Life assurance is not what anyone with money can buy. You are healthy today and so can get an insurance on your life but it might not be possible for you to get an insurance policy some time hence. So many persons are disappointed every year because their proposals for assurance are rejected although most of them could have secured insurance if they had not procrastinated. "There is no one dependent on me," Well, that may be so, but a time will come when you will be dependent on yourself, i. e., during your old age.

Insurable Interest. As already pointed out above, no person can legally effect life insurance unless he has an insurable interest in the life insured. It is essential that the interest should exist at the time the policy is issued. It may arise from a number of causes which may conveniently be grouped under three heads, viz — (a) interest in one's own life, (b) interest on account of blood relationship or marriages, and (c) pecuniary interest. The persons who possess insurable life interest are :—

1. Every person in his or her own life. As life insurance is not a contract of indemnity, there is no limit to the amount for which an insurance on one's life can be effected. But an insurance office shall not accept risk for more than the capitalised value of the income of the insured.

2. A husband in the life of his wife and a wife in that of her husband.

3. A creditor in the life of his debtor to the extent of his claim.

4. A surety in the life of the person for whom he has stood as surety.

5. A son in the life of his parent if the parent supports him but not otherwise.

6. Similarly a parent in the life of the child if he or she is dependent upon the child.

Kinds of Life Assurance Companies. The life assurance business is carried on by limited liability companies which are either *mutual* or *proprietary* concerns. A mutual assurance company is one in which there are no shareholders. Every member of the association is an insurer as well as an insured. The policyholders themselves manage the association for their own benefit. There are no shareholders and the profit is divided amongst the policyholders either in the shape of bonus or in the shape of reduction of premium on the existing policies. In a proprietary life assurance company, on the other hand, there is a distinct class of shareholders from that of policyholders. The former get dividend on their share capital and manage the affairs of such companies. Generally speaking 90% of the profit is distributed amongst the policyholders and 10% goes to the shareholders.

How to Effect Life Assurance. A person wishing to insure his life has,

first of all, to fill up a proposal form. This consists of a number of questions as to the life, habits and antecedents of the applicant. The answer must be given carefully, because the proposal form is regarded as a part of the policy. The insurance company also requires reports of two private friends not related to the proposer and of the insurance agent. It next arranges for the medical examination of the proposer. On receipt of the medical examiner's report, the directors of the company consider the proposal; and if the life is accepted the proposer is asked to pay the first premium. If on an examination of the medical report the proposer's life is found to be normal, his proposal will be accepted at the usual premiums as given in the company's prospectus, but if his life is below standard, he would be required to pay an extra premium.

As soon as the first premium is paid either direct to the Head Office or to a Branch or an agent of the company, the contract is complete and the risk commences. The policy is then prepared and delivered to the assured. The assured is also asked to submit proof of his age. On admission of this proof, the assured must ask the company to issue to him a certificate of admission of proof of his age, otherwise in case of his death his assignee or legal heir shall have to supply this information and prove to the satisfaction of the company.

The policyholder has the right to obtain from the insurance company on payment of a fee not exceeding one rupee a certified copy of the questions put to him and his answers thereto contained in the proposal form and in the medical report supplied in connection with his insurance. This information is likely to prove useful in case a dispute arises over the payment of claim under the policy.

The Policy. The life assurance policy is a contract between the assured and the insurance company. It is issued under the seal of the company and is signed by two directors and countersigned by the manager. It requires a revenue stamp. The policy conditions and privileges are printed on the back of the policy and are incorporated in the body of the contract by reference. The principal clauses of life policy are :—Name of the assured with his occupation and address and his age next birthday, the amount the company undertakes to pay to the assured or his legal representative with or without bonus; the amount of the premium, the date when payable and the days of grace; a clause to the effect that the insured should intimate to the company and pay an extra premium if he takes up some hazardous occupation; conditions under which the policy would be void, e.g., suicide, conditions regarding revival of policies and surrender value, and certain information required by the Indian Insurance Act of 1938.

Payment of Premium. The premium is usually paid annually in advance, but a company will accept the premium in monthly, quarterly or half-yearly instalments, charging a slightly higher rate for the accumulation. The date of payment is set forth in the policy, and a month's grace is usually allowed

beyond the time stated. Companies usually send out renewal notices to policyholders, but a policyholder has no valid excuse for the non-payment of the premium within the time stipulated on the ground that no renewal notice has been received.

It is useful to understand how life insurance premiums are computed. Life insurance is a business quite different from any other kind of business. It needs no capital, it needs no raw material, and it needs no machinery. All that it needs is a certain amount of organisation and a certain amount of propaganda. What factors underlie life insurance premiums? Premium in life insurance is the price that a prospective buyer is required to pay while purchasing a life cover. This price, however, unlike other commercial transactions, is not payable outright. It is payable uniformly over a period of years, the payment ceasing either at the end of a particular period or earlier in case of the death of the assured, the contract becoming fulfilled in the latter case. In the computation of the premium, the following important factors are taken into consideration.

First comes the question of mortality. By mortality is meant the number of deaths expected to happen in each year of age out of certain number of lives of the same age. For example out of 1000 lives of age 20, say 25 may be expected to die at age 21, 24 at 22, 25 at 23, and so on, till a particular age or till the last death. The life insurance contract provides for a certain sum payable on death. The premium that is collected as a price should therefore, be sufficient to meet such payments that may arise in future. This purpose is achieved collectively by charging such a premium to all the 1,000 lives initially and to those who survive every year thereafter, and making payments of the guaranteed sums in cases of death out of the collected amounts. If the experience of mortality justifies the assumption made, the contracts are fulfilled.

Secondly, interest is another factor which enters into the computation of premiums. The number of deaths increases as the age increases. The premium, however, is kept uniform. Thus certain surplus amounts are always available in the early years of assurance to meet the claims in future. Such surplus sums would naturally not be kept idle but will be invested so as to earn interest. The benefit of this interest is given to the lives assured by way of a reduction in the premium, it being assumed that a certain rate of interest will be earned on the surplus funds.

Thirdly, there is the problem of expenses and profits. In order to procure and maintain the business, to collect the premiums in future, to invest the funds and so on, a certain margin of expenses is kept in the premium. This is called the expense loading, which is made on the premium by way of a larger percentage on the first premium (for procurement) and uniform percentage on the renewal premium (for maintenance). In certain classes of contracts, a provision for future profits is made by means of a percentage loading, thereby promising a

future return by way of profits on the business.

Proof of Age. Although a life assurance company does not withhold the issue of a policy until the declared age of the proposer is proved, it is strongly recommended that proposers produce the necessary evidence of age along with the proposal, or as soon after as possible, because it is required before settlement of the claim if the age has not already been admitted. The following proofs are generally accepted :

1. Certified extract from municipal or other records made at the time of birth.
2. Certificate of baptism if it contains age or date of birth.
3. Original horoscope prepared at the time of birth.
4. Certified extract from school or college records if age or date of birth is stated therein.
5. Certified extract from service register in the case of Government employees and employees of quasi-government institutions, provided age has been admitted by such bodies on the strength of birth or school certificates.
6. In the case of a Christian a certificate of birth or baptism or a certified extract from record in family Bible will be accepted.

Commencement of Risk. The risk under a life assurance policy commences on the date of receipt of the first premium in full or the date of acceptance of the proposal, whichever is the later, and the second instalment of the premium falls due on a date calculated from such date of commencement of risk. Policies may, however, if desired, be dated back within the calendar year, for a period not exceeding three months, to give the benefit of calculation of the premium at a lower age.

Indisputability of Life Policies. In terms of section 45 of the Indian Insurance Act of 1938, after a policy has been in force for two years, it will not be called in question on the ground that any statement in the proposal for assurance or any report of a medical officer or referee or friend of the insured or in any other document leading to the issue of the policy was inaccurate or false unless such mis-statement is on a material matter or suppressed facts which it was material to disclose and it was fraudulently made by the life assured and he knew at time of making it that the statement was false or that it suppressed facts which it was material to disclose.

Suicide. In the event of the suicide of the life assured within a year from the date of commencement of the risk, the policy is usually rendered null and void except to the extent of the interest thereunder of any assignee of the policy for valuable consideration who has at least one month previously given notice to the company of his interest in the policy.

Hazardous Employment. If a person whose life is insured enters upon a service or employment or occupation which is materially different from that in which he was engaged at the date of the commencement of the risk under

a life policy, he is usually required to inform the life insurance company of such change, and if the company considers the service or employment or occupation to be hazardous, he may, while so employed or engaged, be required to pay an increased rate of premium.

Exemption from Income-Tax. As an encouragement to thrift and investment an individual insuring his own life or the life of his wife is entitled to a rebate of income tax in respect of premiums paid by him to the extent of one-sixth of his total income or Rs 6 000 whichever is less, provided the amount of the premium does not exceed 10 per cent. of the capital sum assured. A Hindu undivided family of which the policyholder is a member is entitled to a rebate of income tax to the extent of one-sixth of the total income of the family or Rs. 12,000 whichever is less.

Alteration in Policies. A life policyholder may, subject to the production of such evidence as to health and title or otherwise as the life assurance company may require, obtain in lieu of his original assurance an assurance of any other type for the time being granted by the company on payment of a prescribed fee and any stamp duty that may be payable and the difference of premium with interest at a specified rate thereon from the date of his original policy till payment.

Additional Assurance. If within three months of the acceptance of the proposal the assured desires to increase the amount of assurance, he is permitted to do so, without fresh medical examination on production of evidence of good health to the satisfaction of the company, and a new policy is issued for the increased assurance. An application for increasing the sum on the expiry of three months is treated as a new proposal which requires a fresh medical examination.

Lost Policies. The loss of a life policy should be immediately intimated to the life assurance company, with full particulars as to how the policy was lost or destroyed and the steps taken to trace the same. The company will be prepared to issue a certified copy of the policy on payment of a small fee and after due advertisements of such loss or destruction at the assured's cost. In addition a Bond of Indemnity may be necessary.

Revival of Lapsed Policies. Policies under which payment of premiums has been discontinued may be revived to the full sum assured at any time during the life assured. Revival can be effected without medical examination within six months from the due date of the first unpaid premium on payment of the amount of the premiums in arrear with interest there at 7½ per cent. per annum reckoned from the due date of each unpaid premium, subject to a minimum payment of 8 annas. When, however, a policy remains lapsed for not less than 6 months and the premiums in arrear amount to not less than Rs 500, interest will be charged at the rate of 6 per cent only.

After six months from the due date of the first unpaid premium revival can be effected on production of a medical report to the satisfaction of the

directors from one of the authorised medical examiners of the company and on production of satisfactory evidence to show that there has been no adverse change in the personal or family history or occupation and on payment of the arrears of premiums with interest thereon calculated as above compounding half-yearly.

In the event of cessation of payment of premiums after at least three years' premiums have been paid, payment of the sum assured will be made in full in the event of the death of the life assured taking place within six months of the due date of the first unpaid premium under deduction of the company's ordinary revival charge as specified above.

Non-forfeiture Systems. The proposers are usually allowed the choice of one of the following two systems of non-forfeiture:—

1. This is applicable to all classes of policies. It secures automatically to the policyholder and his dependants in the event of cessation of payment of the premiums under his policy a paid-up assurance bearing the same ratio to the original sum assured as the total number of premiums actually paid bears to the total number stipulated for in the policy, subject to the provision that premiums have been paid under the policy for not less than two years and that such proportionate paid-up assurance amounts to not less than Rs. 100 inclusive of any attached bonus. In the case of policies entitled to participation in the profits of the company all bonuses declared and still attaching to the policy at the date of cessation of payment of the premiums remain attached to the reduced proportionate paid-up policy but the policy is not entitled to participate in the profits declared thereafter.

Notwithstanding what is above stated, if after at least three full years' premiums have been paid in respect of a policy, any subsequent premium be not duly paid and the life assured were to die within six months from the due date of the first unpaid premium the policy moneys will be paid as if the policy had remained in full force under deduction of the premium or premiums unpaid with interest thereon to date of death on the same terms as for revival of the policy during such period.

2. Should payment of premiums be discontinued under a policy after it has acquired a surrender value, the company will automatically advance the premiums as they fall due and maintain the policy in force so long as there is sufficient net surrender value (after deduction of any indebtedness to the company with accrued interest) to cover these advances and compound interest thereon at $7\frac{1}{2}$ per cent. Such advance together with interest may be repaid either in whole or in part at any time while the policy is so kept in force. In the event of the policy becoming a claim during this period the claim will be entertained subject to deduction from the policy moneys of the amount so advanced together with interest thereon. If the surrender value is exhausted by reason of such advance and no repayment of the advance with interest is made before then, the policy will lapse and all liability of the company will terminate.

Loans. Loans are granted on unencumbered policies of amounts not more than 90 per cent. of the surrender value but in the cases of policies which are due to mature within 3 years a larger percentage will be granted, the rate of interest charged being at least 6 per cent. per annum payable half-yearly.

The interest is payable along with the premium in half-yearly instalments, and payment thereof is as essential as payment of the premium to maintain the policy in force. The interest falling due concurrently with the premium is payable along with it. Where interest is not paid when due, compound interest will be charged, but if interest is allowed to fall into arrears for six months the policy is liable to be forfeited to the company, subject to such relief as is provided for in the loan bond.

The settlement of loan transactions in the case of policyholders resident in British India will be expedited if application is made direct to the Head Office of the company stating that if the amount desired is not available a loan bond for the maximum amount available should be issued. The application should be accompanied by the policy, any assignment deeds with the names and ages of the assignees and a remittance for the amount of the stamp duty calculated at the rate of approximately annas 12 for each Rs. 100 of loan desired.

Settlement of Claims. In the case of claims occurring by the death of the life assured, the claim is paid after proof of death and proof of the title of the claimants to the policy moneys have been produced to the satisfaction of the insurance company. In the case of claims occurring by maturity of the policy, the life assured is advised by the insurance company well before the actual date of maturity in order that the necessary papers may be completed before the payment is made on the date of maturity.

The proof of death is furnished by submission of any of the following certificates:—(a) certificate from the doctor who attended the deceased in his last illness; (b) certificate of registration of the death by the registrar of deaths; (c) certificate from employer identifying the deceased, (d) certificate of identity from a responsible person acquainted with the deceased.

The proof of the title of the claimants to the policy moneys is required in all cases where a policy has not been assigned nor is a nominee appointed by the life assured during his lifetime. The proof of title may be in the form of a probate of will or letter of administration granted by a High Court, or it may be in the form of a succession certificate granted by a District Judge.

Every company is compelled to obtain such proof of title of the claimant to the estate of the deceased policyholder before payment of the claim, both to comply with the law and to ensure that the policy moneys reach the hands of whomsoever is entitled by law thereto. In terms of Section 47 of the Insurance Act, 1938, a company may apply to pay into court the moneys due under a policy within a specified time from the date of maturity or from the date of intimation

of death if the claim cannot be settled by reason of conflicting claims or insufficiency of proof of title or for any other adequate reason.

Assignment or Nomination of Policies: In view of what is stated above, policyholders are strongly advised either to assign their policies during their lifetime to whomsoever they wish should benefit their policies or to nominate the persons to whom the policy moneys are to be paid in the event of their death. Forms of assignment and nomination are printed in this prospectus and a memorandum of instructions is issued along with the company's policies.

Policies may be assigned by the policyholder to anyone for valuable consideration or to anyone within his immediate family circle for love, favour and affection. A separate form of assignment of either nature may be obtained on application to the company. Unless otherwise provided by any law in force at the place of execution of an assignment, policyholders should give notice in writing of assignments since no assignment will be operative against the company until such notice is received. This is further necessary since priority of claims under assignments will be governed by the order in which notices are received by the company.

A nomination, if not incorporated in the text of the policy itself, can be made only by an endorsement on the policy but such nomination to be effectual must be communicated to and registered by the company for which purpose the policy bearing the nomination must be sent to the company. A nomination may be cancelled or changed by an endorsement or a will before the policy matures for payment. Notice in writing of any cancellation or change of nomination must be delivered to the company, failing which the policyholder takes the risk of payment of the policy moneys to an earlier nominee either mentioned in the text of the policy or registered in the records of the company. An assignment automatically cancels a nomination subject to the proviso that the assignment of a policy to the company in consideration of a loan granted by the company on the security of the policy or its reassignment on repayment of the loan will not cancel a nomination but will affect the rights of the nominee only to the extent of the company's interest in the policy. It has to be noted that a nomination will not give the same protection against creditors as an assignment ordinarily would. A fee of Rs. 1 is usually charged for each nomination subsequent to the first.

It should be noted that a nomination or cancellation or change thereof can be validly made only in British India unless the law of the country or State outside British India where such nomination or cancellation or change thereof is made also permits it.

In registering an assignment or nomination or notice thereof, the company makes no admission and expresses no opinion whatever as to its validity or effect, it being understood that the parties satisfy themselves as to the form of assignment or nomination, amount of stamp duty on assignment and all other

points relating to the assignment or nomination before sending it to the office for registration

Kinds of Life Assurance Policies

The kinds of life assurance policies issued by present-day insurance companies are numerous, and novel methods of assurance are being continually introduced, but the principal types of life assurance policies are :—

1 **Whole Life Policy** This is a policy under which the sum assured is to be paid only on the death of the life assured. The premium on a whole life policy may be payable in one instalment, or for a specified number of years, or up to the attainment of a certain age. In the first case, the policy is known as a '*Single Premium Policy*'; in the second case, it is called a '*Limited Payment Life Policy*'; and in the third case, it may be called a '*Special Whole Life Policy*'. The single premium life policy is not popular, because ordinary person cannot afford to pay the whole premium in one lump sum, and in the event of early death the assured will be a loser. A whole life policy may be a '*With-Profits*' or a '*Without-Profits*' Policy. The holders of with profits policies are entitled to a share in the profits of the company in addition to the sums assured, whilst the other class gets only the sum assured.

The share in the profits of an assurance company which the with-profits policyholders receive is known as '*Bonus*' which may be declared if the periodical actuarial valuation discloses a surplus. Bonus to with-profits policyholders may be paid in several ways. It may be paid in cash immediately after its declaration. It may be added to the amount of the policy each time and the policyholder will receive it when the policy becomes a claim. It may also be utilised in reduction of premiums to be paid.

The ordinary whole life policy on account of its low premium recommends itself to at least two fairly well-defined classes : (a) those receiving relatively small incomes, and (b) those who receive moderate but certain incomes during the productive years of their lives and who have large family obligations. They are able on account of the low premiums to carry a large amount of insurance during the period of dependancy of the children, and beyond this period the premiums may either be paid in part by the children of the policies surrendered or changed to paid-up insurance, assuming that the policyholder is not financially able to keep up the payments. The ordinary life policy of a present-day insurance company has so many privileges in the contract and is so excellent in its general character that it is a great misfortune, both to the public and the insurance business, that it is not more frequently sold. This policy will, however, become more popular if the public and the insurance officials become divorced from the idea that insurance is an investment.

The limited payment life policies commend themselves to those individuals who desire their premium payment period to be confined well within their productive years. This policy will appeal to the young man who is

uncertain of an income after a given period or who does not wish insurance to be a part of his annual expenses after middle life. Out of the relatively large and certain income of his early productive years, he pays for his insurance. He has the satisfaction of realising that he has purchased and paid for the protection which his family has a right to expect from him. This policy is also often selected by the man of middle age who has previously neglected to purchase protection, but who wishes then to buy it and pay for it while he is yet a producer. The ordinary life policy premium may cause an undue pressure on the decreasing income of his declining productivity.

2. Endowment Policy. This is a policy which provides for the payment of the sum assured either on the attainment of a specified age or at previous death. This kind of policy thus combines two risks and therefore two premiums—the premium for the temporary assurance and the premium for the endowment on reaching the specified age. Consequently the premium for an endowment policy is higher than that for an ordinary whole life policy. An endowment policy may also be a with-profits or without-profits policy.

Many life insurance companies also issue what is known as the "*Double Endowment Policy*". This plan of assurance provides for payment of double the sum assured on the survival of the life assured to the selected term of years; but in the event of his earlier death, the sum assured alone is payable.

Under an endowment policy the premiums are payable for the number of years selected or up to the specified age or until death if it occurs earlier.

The endowment policies commend themselves to those who desire to have, in addition to the protection, a material incentive to save. The premiums are considerably higher than those for ordinary whole life policies. They not only afford a means of saving for the young man, but they also mature at a time when the individual, as a result of his larger business experience, is often better able to make profitable investment of large funds. If past investments have been wisely made from other savings and the individual does not need the amount of the policy for current use, he may purchase a considerable amount of paid-up assurance because his insurance premiums have been large. Again the policy has larger loan values than any other policy, and this sometimes becomes an advantage for the young person. The argument that the individual could secure a better return if he would invest his savings in a savings institution is more interesting than true, because the average individual will not save regularly unless under pressure. No one compels him to go to the savings bank to make his deposits and no one prevents him from withdrawing them at his pleasure.

3. Joint Life Policy. A policy may be effected upon the joint lives of two or more partners so that in the event of one of the partners dying, the capital taken out of the firm consequent upon his death may be replaced by the proceeds of the policy. The premium on such a policy would be paid out of the partnership monies, and the policy would form part of the partnership

assets. In the event of the partnership being dissolved, the surrender value of the policy could be distributed amongst the partners in the same way as the other assets.

The sum assured under a joint life assurance policy is payable on the first death of either of the two lives assured.

4. Educational Annuity Policy. This policy is intended to provide for the education of one's children. The person to be medically examined is the parent or guardian on whose life the policy is to be taken out. The premiums are payable for the term of years selected or only till the death of the parent or guardian if earlier.

In the event of the child's death prior to the date of maturity while the policy is in force, all premiums paid excluding the first year's may be refunded to the parent (or in the event of his previous death to his legal representatives) or the parent may if he so desires, continue the policy by substitution of the name of another child.

The educational annuity is payable to the parent if alive, otherwise to the child if of age, but if not, to his legally appointed guardian, for a period of five years, in half yearly instalments, the first instalment being paid on the survival by the child of the selected term of years. In the event of the death of the child after the instalments have become payable to the parent, but before payment of all the instalments have been completed, the balance of the instalments will be commuted at a certain rate of interest and paid to the parent falling whom to his legal representatives.

5. Marriage Endowment Policy. This policy is intended to provide for the marriage of one's children. It is to be taken out in the same way as an educational annuity policy. The sum assured under this policy is payable to the parent if alive; otherwise to the child if of age, but, if not to his legally appointed guardian. The surrender value of a policy effected under this plan is usually guaranteed to be 90% of the annual premiums paid excluding the first year's.

6. Children's Deferred Assurance Policy. This class of a policy is designed to enable a parent or guardian to secure for his child or ward the benefit of an endowment assurance at a considerably low cost, irrespective of the condition of the health of the child at the date of the commencement of the risk.

This is an endowment assurance issued usually on the lives of male children who have completed one year of age but have not completed 18 years, providing the payment to them of the sum assured at the end of a selected period or at prior death after the deferment period (i. e., the interval between the date on which the policy is taken out and the policy anniversary just preceding the attainment of age 21). If the child dies during the deferment period all premiums paid excluding the first year's are returned with interest at 2½% per annum compounded yearly. On termination of the deferment period, the policy

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can be surrendered for a cash payment which will be equal to 90% of the premiums paid excluding the first year's with interest at 2½% per annum compounded yearly or the total premiums paid whichever is greater.

No medical examination is necessary unless the child's age is 17 years or over next birthday.

If the proposer desires to discontinue the policy during the deferment period, he is entitled to a surrender value provided the policy has been in force for at least two years. The surrender value available in these cases will be 90% of the premiums paid for the complete years during which the policy has been in force excluding the first year. After the deferment period the surrender value will be higher than the amount payable under the similar class of assurance taken out at age 21 for the same number of years after the commencement of risk. It is quoted on application to the insurance company.

If the proposer dies during the deferment period, the guardian of the child can continue the payments. The policy will automatically be the property of the child after the deferment period. During the deferment period the policy will be under the full control of the proposer. If he dies in the mean-while it will be under the control of the legally appointed guardian of the child.

The policy begins to participate in profits after the deferment period, if it is a with-profits policy.

During the deferment period, after at least two years' premiums have been paid, if any further premiums be not paid the policy will remain in force reduced to such proportion of the sum assured thereunder as the number of annual premiums paid bears to the total original number stipulated for. After the deferment period the paid-up amount will be quoted on application to the insurance company.

7. Perfect Protection Policy (also called as Family Income Policy or Ideal Security Policy). Life assurance is a necessity to every married man who desires to make provision at his death for his wife and family. It enables provision for their maintenance and the education of the children to be made at a very small annual cost. Hitherto life assurance contracts have not been specially framed to meet the critical situation which may and often does arise in the first 20 years or so of married life when resources are taxed to the utmost to meet the cost of the maintenance and the education of a young and growing family. It is also doubtful whether life assurance contracts have in the past been framed recognizing that the average widow is inexperienced in the handling of large sums of money and is generally dependent on an outsider for the investment of the policy moneys when these are received from the assurance company.

In India, as in other countries, many unscrupulous persons ready to take advantage of such a situation undoubtedly exist, and it is primarily to prevent such persons laying hands upon and so prevent the squandering of the assurance money as well as to provide the necessary provision during the critical period

of the widow's life-time that such a policy has been devised.

The policy is intended mainly for the young man just starting married life and provides, in the event of the assured's death during the first twenty years of the contract, a guaranteed income, equal to 10 per cent. per annum of the amount assured, payable from the date of the assured's death until the expiry of 20 years from the inception of the contract, when the sum assured itself becomes payable in full. Thus the widow and family can be guaranteed an adequate income until in most cases the eldest child has attained majority and the widow is relieved from all trouble and risk involved in arranging for a safe and remunerative investment of the policy money's during the period in question.

The policy further provides for payment of the sum assured in full in the event of the assured's death occurring after 20 years from the inception of the policy. It is recognized that by such time the expenses connected with the maintenance and education of the family should no longer be so heavy and the provision ensured by payment and investment of the sum assured should be sufficient for future needs.

The perfect protection policy can be effected either with or without participation in profits. If effected with participation in profits, the bonus additions attaching to the policy will be payable on the death of the life assured.

It is claimed that the policy is the most up-to-date of its kind and that it provides the most practical form of protection obtainable for the wife and family. Husbands and fathers are asked to consider the special risk to which practically every family is exposed during the first 20 years of married life, and then see how that risk is covered by the following benefits which are provided by such a policy of Rs. 10,000 :—

(1) In the event of the husband's death within 20 years from the inception of the policy :—

- (a) A guaranteed income of Rs. 1,000 per annum to be payable by monthly instalments of Rs. 83.5.4 until the end of the 20 years period, the first instalment to be payable one month after the death of the assured ;
- (b) Rs. 10,000 in cash at the end of the 20 years period to meet, if required, the cost of the higher education of the older children or to start them in business as well as make provision for the future maintenance of the widow and younger members of the family.

(2) In the event of the husband's death after 20 years from the inception of the policy :—

- (a) Rs 10,000 to be paid on the death of the husband for the future maintenance of the widow and family, the older members of which by that time should be no longer dependent on the life assurance provision.

Subject to proof of death, title and age, the first instalment of the guaranteed monthly income will be paid one month after the death of the

assured, and the last instalment on the same day of the month immediately preceding the expiry of the period of 20 years from the inception of the policy.

Life Assurance with Disablement Benefit. A notable extension of life assurance benefits is now being offered by some companies in the form of provision against loss by forfeiture of life assurance resulting from inability to continue payment of the premiums consequent upon sickness or disablement. Life assurance is generally recognised by every prudent man as the best means of providing for his family and dependents; but how insecure is that provision unless the assured is reasonably sure of being able to continue the premiums; and how great is the danger of his being unable to do so as a result of prolonged illness or a serious accident! Most salaried business and professional men have no cause for financial worry in the event of an incapacity lasting several months only, but beyond that period the matter may cause serious financial embarrassment, which can be averted by combining life assurance with disablement benefits.

On payment of a small extra premium, some companies policies provide for the waiver of premiums upon proof of total and permanent disability of an insured life (not following hazardous occupation) through accident occurring prior to age 60 and for payment of double the sum assured in the event of accidental death of the life assured within the premium-paying period before age 60 where death occurs within ninety days of the injury.

Non-medical Life Policies. The Superintendent of Insurance made the following suggestions in the *Indian Insurance Year Book* of 1944 regarding the issue of life policies without medical examination:—

One direction in which insurers can practice economy is by the issue without medical examination of policies of which the sum assured does not exceed Rs. 1,000 to begin with. An enquiry made by the writer into the duration of persistence of medical selection in connection with an investigation into the mortality experienced by those insured with the Oriental Government Security Life Assurance Company covering the decennium 1925-1935 has proved beyond doubt that the effect of medical selection on lives assured does not on the average last for a period much more than one year. There is no reason to assume that the experience of other insurers in this respect should be different from that of the 'Oriental' and this may be assumed as a feature, at least for the present, of medical selection for assurance purposes in India. This being the case insurers would not be taking any great risk if they transact non medical business subject *inter alia* to the following conditions:—(1) The sum assured does not exceed Rs. 1,000; (2) A declaration of good health is taken in every case and properly scrutinised; (3) In case of death in the first year a part of the premiums paid alone is returned according to a sliding scale; and (4) The papers relating to the personal and family history of the proposer are subjected to a very careful scrutiny and the insurer reserves the right, in case where these are not entirely satisfactory, to call for medical examination.

This would call for concerted action on the part of all insurers. After investigating the experience acquired by the issue of non-medical policies for Rs. 1,000 over a period of, say, 5 years and finding it satisfactory, insurers may extend the principle to policies not exceeding Rs. 2,000, and the writer does not advise extension of the issue of non-medical policies for sums assured exceeding Rs. 2,000 for a considerable time.

Selection of Life Insurance Company

When a person wishing to insure his life has made up his mind as to the policy or policies that will best meet his requirements, he must select the company or companies in which to insure. He may like not to put all his eggs in one basket, and it is good thing not to do so.

Whether the hope with which life assurance is effected will be realised or not depends upon the soundness of the company with which the insurance is effected. It often happens that a person insures his life, pays premiums by stinting himself, but ultimately the company fails and he gets practically nothing. The stability of the company is, therefore, a very important factor in the matter of successful insurance. Every man cannot, however, be a judge of the stability of a company. He is most often dependent upon the agent of the insurance company. The insurance agent is interested in himself. With an increase in the number of companies doing life assurance business in India, the number of insurance agents has also considerably increased. They go from door to door and canvass for their respective companies. Sometimes they manage to get hold of some persons who are influential in their own circles and through them, push forward their business. The number of those who go in for life assurance after weighing the merits of the different companies is comparatively very small. The majority consists of those who take out their life policies from a company simply because they are approached by that company's agent first.

It may be said that life assurance in India is more often sold than bought. Only in a very few cases, anything like a proper selection of a life office is made. The seller, who is usually the agent of a company, places before the buyer (i.e., the would-be policyholder) the good points of the company he represents, keeping back as far as possible other important aspects of the company, a knowledge of which is essential in forming a correct idea of the company's soundness. A majority of buyers of life assurance in this country not being well-versed even in the elementary technique of life assurance business, are not in a position to sieve good companies from bad.

It is true that the Indian Insurance Act of 1938 had laid down conditions whereby unsound insurance companies will be gradually eliminated from continuing in operation. Although this Act has made it almost impossible for unsound concerns to come into existence, yet it must not be supposed that it has made all the existing insurance companies sound. There are companies and companies.

When it is desired to select a life assurance company for insurance, the following points should be carefully considered :—

1. **Business Methods.** When one thinks of over three hundred institutions vying with one another in a scramble for business, one can well realise how keen competition is and how near it comes to a veritable struggle for the survival of the fittest. It behoves all responsible persons to see that the business of insurance is in proper hands and is being conducted with due consideration for the interests of the insured. Quality and not quantity suggests itself in a matter of this kind. There are number of life insurance companies in India which are not suitable concerns to handle such a highly technical business as life assurance. Pandit Jawaharlal Nehru once said, in reference to insurance enterprise in India that "we must build our sawadeshi industry on the rock of efficiency and not merely on sentiment".

The price of insurance, namely, the premium, is of a complex character being based on certain assumptions regarding the future working of the insurance company. A prospective customer should therefore try to obtain information on the working of those factors before choosing a particular company. The factors are mortality experience, interest earned and expenses. The inquiry should be of the following nature and the information will be available in the company's published accounts :—

(a) Is the mortality experience of the company within the expectation underlying the premiums and also the last valuation basis? How does this experience expressed as a percentage compare during the last few years with these assumptions?

(b) Is the experience as regards the interest earning of the funds favourable, and, if so, how does it compare with the assumptions made in the last valuation and also in the premiums during the last few years?

(c) What is the experience of the company regarding its expenses? Is the expense ratio within the provision made in the last valuation? Usually in a valuation, provision for expenses and future profits is made in the aggregate by way of a percentage of the premium. It would therefore be helpful to know as to what extent the expense ratio of the company for the last few years is below the valuation provision, particularly because the lower it is than the provision, the larger will be its contribution to the profits of the company. If a company gives little or no thought to the restriction of expenses within the provision of the premiums, then the business is being written at a higher cost than the premiums will stand, and the results are inevitable.

2. **New Business.** Ascertain the amount of new business secured by the company during the last year, and inquire into its quality and cost. Slow and steady growth is to be preferred to a forced march in the matter of securing new business. A decline in business may sometimes be the result of deliberate policy of the management by accepting only quality business.

Big figures should not, however, lead one to assume that a large expan-

sion of new business is the *sine qua non* of life assurance or that it is the sole criterion by which a life office should be judged. On the contrary, unless new business can be obtained at a reasonable cost and conforms to the requisite standards of quality, its procurement would be detrimental to the interests of existing policyholders.

3. Lapse Ratio. The percentage of lapses, the bane of life assurance business, should be noted. An improvement in the lapse ratio can be due only to a careful selection of lives and constant service, whereby the policyholders are encouraged to keep their contracts in force.

4. Bonus Record. Has the company been able to declare profits in its last valuation, and if not, is there any prospect of a future declaration? This question is necessary in view of the profit margin in the with-profits premium, which is collected from the policyholder with an implied promise of returning the same by way of future bonuses. It may happen that a company may not have declared a bonus as a matter of conservative policy but there may be future prospects of a bonus. In this connection the following extract from the Chairman's speech delivered at the extraordinary general meeting of the Oriental Government Security Life Assurance Company, Ltd., held on 2nd October 1940, is to the point:—

"I should not be misunderstood when I say that the mentality of the Indian insuring public has been unfortunately trained to attach more importance to bonus than to the security of the primary benefit represented by the sum assured itself. This has created an unhealthy race amongst companies for declaration of progressively increasing bonuses without regard to the capacity of the companies to earn these rates. I should like to stress that the time has now arrived for insured persons present and prospective to think less of bonus and more of the sum assured. The anxious times created by the fall in the rate of interest have provided an opportunity for all companies to take stock of the situation and strengthen their valuation bases in conformity with the actual investment conditions obtaining in the market so as to safeguard for the lives assured and their dependents the sum assured which is the main benefit afforded by a life assurance policy."

During the last few years, with a falling rate of interest and a higher ratio of expenses, the valuation results have naturally disclosed hardly any surplus, and most of the companies have had to pass over the bonus. Even the companies that have declared a bonus have been able to give only a reduced one, which is very much less than what they were accustomed to pay before.

5. Financial Position. The first and the most important factor essential to a good life assurance company is that of security. A life assurance company is essentially a credit institution. Its intrinsic soundness is of more importance to the policyholders and the insured public than the volume of business it underwrites or the size of its funds. The layman is apt to be imposed upon by large figures.

The assets must be sound, secured and properly valued. There must be well-planned distribution of the assets consistent with the two canons of safety and adequate yield. There can, of course, be no hard and fast rule regarding the distribution of assets of a life assurance company. Much depends upon the peculiar circumstances of each individual office. See if there are any inner reserves on the Balance Sheet.

6. Investment Policy. The investment policy of a life assurance company is now governed to a large extent by section 27 of the Indian Insurance Act of 1938 : but still some discretion is left to the management in this matter. Under the conditions prevailing in India, the investment policy should satisfy the two well-known canons, namely, absolute safety consistent with the maximum yield.

The investments should be properly distributed among all classes of recognised securities, such as Government and trust securities, first mortgage on building property at a comfortable margin yielding satisfactory interest income, preference shares and debentures of public utility companies and other reputable industrial concerns, etc. The whole idea of the investment policy should be the diversification of risk and the averaging of yield.

With the present limitations on investments imposed by section 27 of the Insurance Act, there is very little scope indeed for investment in industrial concerns. Under this section 55 per cent. of the life insurance fund of a company has to be invested in Government and trust securities. Usually about 10 to 15 per cent. are given as policy loans and about 5 to 10 per cent. are invested in building property, leaving only about 15 to 20 per cent. available for investment in industrial concerns or other public companies. It should not, however, be considered that every hare-brained scheme that comes forward should be funded by the insurance companies or that new ventures should be allowed to be patronised by life insurance offices. But some of the funds of life insurance companies may very well be invested in well-established concerns and in well-secured debentures of even newly-started companies.

7. Policy Conditions. The policy conditions should be liberal and should include all up-to-date privileges such as disablement benefit, etc. The actual conditions of policies issued by various companies are different; and therefore it is necessary to examine carefully the policy conditions before choosing a life office.

8. Management. A life assurance company requires capable and experienced management; it is not everybody who can run a life office successfully. It is all very well to argue that what others have done from small beginnings can still be done. Conditions have changed materially and it is more difficult now to make a success of a new life insurance company. Besides, in insurance the test of time is what counts, and most companies have yet to stand that test. Business pouring in and big figures to show to the public do not always spell success. Time alone will tell what the quality of the manage-

ment is and what security has been built up for the policyholders.

Fire Insurance

The contract contained in a fire insurance policy is an agreement by which the insurer in consideration of a suitable premium undertakes to make good by cash payment or otherwise any loss sustained by the insured through damage or destruction by fire of the property detailed and described in the policy, upto an amount not exceeding that set forth therein. It is understood that the description of the property given in the policy is correct and that all facts material to the insurer's estimate of the risk involved have been disclosed, and also that the insured's interest in the subject-matter is a legal one. The three cardinal principles of a fire insurance contract are as follows :—

- (1) The contract is one "of the utmost good faith".
- (2) The contract is personal to the insured and the insurer.
- (3) The contract is one of indemnity.

Good Faith. In legal phraseology, a fire insurance policy is a contract *uberrimae fidei* (of the utmost good faith). By this is meant that each party to the contract, the proposer on the one side and the insurer on the other must make full disclosure of all facts that are material to enable the other party to understand the nature and extent of the contract into which he is entering.

As regards the insurer (whether a company or an individual underwriter) the matter is simple; the meaning of the policy that is offered must be made clear. For example, the prospectus or proposal form must not suggest one thing and the policy give something different or be hedged with unreasonable restrictions of which no indication was suggested when the negotiations were in progress.

On the part of the proposer, the obligation is more onerous. *Uberrimae fides* requires that he should make the insurer acquainted with all facts that it is necessary for him to know in order to enable him to decide whether or not to insure the risk offered, and, if he decides to accept it, the premium to be charged. The proposer need not draw attention to facts that are either common knowledge or are part of the special knowledge that all fire underwriters may be presumed to possess. He need not, for example, point out that petrol is to be found in the tanks of motor-cars or that glue is likely to be heated in a carpenter's shop, although both of these facts are material to the underwriter in his judgment of a risk. The proposer must, however, divulge any material fact that does not come under these headings. This onus is not removed, although as regards physical hazard it is lessened, by an inspection of the premises by the insurer's surveyor.

It is easy to see why the requirement of full disclosure is essential. The circumstances of a risk are known best to the proposer and some of them can sometimes be known to him only. If he were not bound to reveal all important features, the underwriter would frequently be seriously misled in his estimation of the hazard.

Among facts which must be disclosed are that the risk of fire is greater than is ordinarily the case; that the proposer has had previous fires; that the proposer is actuated by some motive other than ordinary prudence in seeking insurance; that threats have been made to burn down the property and that renewal of the insurance has been declined by other insurers. Any fact not otherwise material becomes so on being made the subject of a specific question.

A Personal Contract. One of the most important facts with which an underwriter wishes to acquaint himself before deciding to accept a proposal for fire insurance is the character and standing of the proposer. If the "moral hazard" is not satisfactory, he will not issue a policy, however high a rate of premium may be obtainable. It is consequently not surprising to find that a fire insurance policy is a contract that is personal to the insured and the insurer, that is to say, the interest in a policy cannot be transferred by the insured to another party without the consent of the insurer. There are, however, a few exceptions to this rule. When property passes by will or by "operation of law" i.e. by the appointment of receivers in lunacy, the protection of the public companies or of receivers or committees in lunacy, the protection of the policy is automatically transferred to the new interests. By recent legislation, too, the prospective purchaser of a building, but, out of movable property, is to be held insured jointly with the vendor during the currency of negotiations. This provision merely makes universal and compulsory what had become a common practice of insurance companies. When the purchase is completed and the interest passes entirely to the purchaser, the insurer can refuse to continue the contract.

Indemnity. The keynote of a fire insurance policy is that it is a contract of indemnity. Although agreeing that this is technically the position, leading business men have been known to dispute the legality of agreement on the grounds that it is not equitable. It was contended that if a person proposed to insure his property for a reasonable figure and the insurance company was not only prepared to accept but actually took premium calculated on this figure and continued to do so for several years there was an implied acceptance of the insured value.

Examining this contention on the surface it appears reasonable. A superficial examination, however, of any subject, as often as not results in an improper conclusion. It has long been understood that honest people carry a heavy burden by reason of the dishonest people inflicted upon them and the analysis of so complex a subject as insurance without taking into consideration the existence of malfeasance is sheer waste of time. It is the honest people who have to pay for the upkeep of our jails regardless of the fact that they themselves may have no direct interest in their maintenance. As regards insurance it is the honest man who must here also pay for the activities of the dishonest.

The prime consideration of a fire insurance company is that a policyholder should not derive a profit from a fire. To explain why this is so is unnecessary. The reason bluntly is that there are too many people in this world unable to restrain themselves in the face of such possibilities. Insurance companies have consequently been obliged to protect themselves by stipulating that the insured value is the replacement value with like kind and quality at the time of loss. Insurance companies further protect themselves by reserving the privilege of reinstating property "which is the subject of a claim."

This is a subject which has received the careful attention of both the insuring public and insurance companies for something over a century and the present system is undoubtedly the most equitable for everyone concerned. As far back as the middle of the last century the fundamental principles of fire insurance were summed up in an Irish Court when the learned judge said,

"It has been truly stated that a policy of insurance is a contract of indemnity and that, while the insured may name any sum he likes as the sum for which he will pay a premium, he does not, by so proposing that sum, nor does the company by accepting the risk, conclude themselves as to the amount which the plaintiff is to recover in consequence of the loss, because, although the plaintiff cannot recover beyond the sum insured in each particular item, he cannot recover even that sum unless he proves that he has sustained damage, and then he will recover a sum commensurate to the loss which he has sustained."

Life versus Fire Insurance. If we compare the contracts of life and fire insurance, we find that a life policy is obtained for a longer period, whilst a fire policy may be obtained for a period ranging from 10 days to 12 months. On the expiry of this period the fire policy can, no doubt, be renewed with the approval of the insurance company and on payment of a fresh premium. In the life assurance contract both the elements of protection and investment are present, but in the case of fire contracts there is only the element of protection. The classification of risks in life assurance is simpler than in fire insurance, and consequently the rates of premium in fire contracts differ very much. Unlike a life policy, a fire policy has no surrender value. The insurable interest in a life assurance must necessarily be present at the time of entering into the insurance contract, while in case of fire it must be present both at the time of entering into the contract as well as when the loss takes place. There is a greater moral risk in the case of fire contract than in a life. Then again, unlike a life policy a fire policy cannot be assigned without the consent of the insurer.

Here one difference with marine insurance may also be noted. A holder of a marine policy may recover not only the value of the goods lost or damaged but he can also ask for compensation including the profit which he would have otherwise made, had the goods been sold in the market. But in fire insurance the insured cannot make any profit on the goods destroyed. He is entitled only to an indemnity pure and simple.

Insurable Interest. In common with all kinds of insurance, the insured must have an insurable interest in the subject-matter of the contract. As a rule, any existing right amounts to an insurable interest. An owner can insure his own goods, an agent the goods of his principal, a trustee the property which he holds in trust, a common carrier the goods which come into his possession in the ordinary course of his trade. One insurance company has a sufficient insurable interest in the property insured with it to reinsure it with another company. A mortgagee has such an interest in the property mortgaged.

How to Insure. The first thing to be done would be the filling up of a proposal form which is in effect similar to that used in life insurance. The utmost good faith is required in filling up this form. All material facts should be fully disclosed and correctly described. When deciding the amount for which the property is to be insured it should be remembered that in the event of a fire, only the amount of the actual loss can be recovered from the insurer. Therefore there should be no overvaluation except for the probable rise in price during the period of insurance.

The insurance company will then consider the proposal, make its own examination of the property and quote the premium for the risk. It is almost impossible to fix fire insurance rates with the mathematical precision with which life insurance premiums are computed. The fixing of fire insurance premiums is a difficult and complicated matter, and depends upon a variety of circumstances, such as the construction and situation of the premises, the nature of the trade carried on, the character of the goods insured and other similar things.

Tariff and Non-tariff Offices. A great part of the fire insurance business is transacted by 'tariff offices' which are members of the Fire Insurance Association for a particular area and which conduct their business in accordance with the rules of the association. The association fixes the rates for the various kinds of serious risks and secures that adequate premiums are charged for the various risks insured against. This combination prevents undue competition amongst the insurance companies. Non-tariff offices, on the other hand, are outside the control of the association. They assess each risk on its merits and charge premiums accordingly. But such offices are not many.

Fire Insurance Policy. On payment of the premium the insurance company issues a 'cover note', from the date of which the risk commences. The policy is prepared afterwards. It is signed by a representative of the insurance company, bears a revenue stamp, and contains the name and address of the insured, full description of the property covered and the amount insured in consideration of the premium paid. On the back of the policy are printed the various conditions under which insurance has been accepted by the insurer. The main conditions are as under :—

1. Misdescription, misrepresentation or omission renders the policy void.
2. Changes in the risk to be notified and the company's assent to be obtained by endorsement on the policy

3. The policy not to cover (a) goods held in trust or on commission, (b) china, glass, jewels, manuscripts etc., (c) deeds, bonds, bills of exchange, money, (d) explosives or loss through explosion, (e) loss through spontaneous heating, (f) loss through earthquake, enemy, riot, etc.
4. If the property insured passes to another person the policy to cease to be in force unless the company endorses the policy to the contrary.
5. Immediate written notice of loss to be given to the company and written particulars of claim to be sent within 15 days.
6. If the claim is fraudulent, all benefits to be forfeited.
7. The company has the right of reinstating the property damaged or destroyed instead of paying for the loss.
8. The company may enter the premises where loss has occurred and may remain in possession or remove property insured.
9. The company to be liable only for a rateable contribution if there exists double insurance.
10. The average clause will be applicable, if other insurance of the same property is subject to average.
11. Any dispute about the claim to be settled by arbitration.
12. If policy becomes void, the premiums paid to be forfeited.
13. The company's printed receipt is the only valid one.
14. The insured to assist the company in enforcing any claim the company may have on other persons.
15. Non-compliance with any warranty to be a bar to any claim under the policy.

The Average Clause. Average is a word of rather uncertain history. It comes to us through the French from the Latin *habere*, to have, and possibly, although not certainly its earliest meaning was service rendered to a feudal lord in carting his wheat. Later it came to mean a charge for cartage, then a contribution in proportion to a man's possessions towards the value of things lost during carriage. From this stage the transition is easy to its present-day usage in insurance, where it is employed in three different senses, in addition to the ordinary signification of a mean of value or quantity.

The first and most familiar use is in the phrase "the law of average". Insurance is often said to be founded on the law of average, actually it is based neither on a law nor on average, but on the theory of probabilities, which shows how the chances of the occurrence, or recurrence, of fortuitous happenings may be calculated. The word average is, therefore, misapplied.

The second use is in marine insurance, where average has come to mean both damage done by perils of the sea and a contribution to a loss or charge incurred (to quote the standard definition of "general average") "for the purpose of preserving the property imperilled in the common adventure."

The third use of the word is in the "conditions of average," which are found at times in fire, burglary, and some other policies, and it is with this aspect of the subject that we are concerned here.

When fire insurance became systematized in the late seventeenth and early eighteenth centuries, it was soon found necessary to prevent the owner of two or three separate buildings or other lots of property from insuring them for a sum sufficient to cover one only, trusting to the probability that not more than one would be burnt at any one time. A clause was then devised, providing that in the event of underinsurance the policy-holder should bear a proportionate part of the loss. This clause was called the average clause.

The average clause now most commonly used (sometimes known as the *pro rata* condition) runs as follows—

Condition of Average. Whenever a sum insured is declared to be subject to Average, if the property covered thereby shall at the breaking out of any fire or at the commencement of any destruction of or damage to such property by any other peril hereby insured against be collectively of greater value than such sum insured, then the insured shall be considered as being his own insurer for the difference and shall bear a rateable share of the loss accordingly.

This is the true average and its operation is simple. If a person owns property worth Rs. 10,000 and he insures it for Rs. 7,500, and if it is damaged by the contingency insured against to the extent of Rs. 4,000, the settlement under a policy bearing the average clause will be as follows—

Company pays $7,500/10,000$ ths (or $\frac{3}{4}$) of Rs. 4,000 = Rs. 3,000

Insured pays $2,500/10,000$ ths (or $\frac{1}{4}$) " " = Rs. 1,000

If the average clause had not been in the policy, the company would have had to pay the whole loss.

Importation of Average. No insurance is subject to average unless it is so declared in the policy, with one exception. If property is insured in more than one office and any one of the policies is subject to average, then average is "imported" from it to all the other policies and they are interpreted as if they had borne the average clause in the first instance.

Exceptions in Fire Insurance. A fire insurance policy does not cover damage caused by fires arising in any way nor does it cover property of every description. The excluded causes of fire and the excluded classes of property are set out in the policy, and are technically known as the 'exceptions'.

The risks which an ordinary fire insurance policy covers are loss or damage caused by (a) fire, (b) lightning, (c) explosion of boilers used for domestic purposes, and (d) explosion of gas (elsewhere than in gas works) used for domestic purposes.

The risks which are not covered by an ordinary fire policy are:—(a) explosion other than that of gas as mentioned above, (b) fires caused through spontaneous heating or fermentation of the property insured, (c) fires caused by the property undergoing a heating process, and (d) fires caused by earthquake.

riot, civil commotion, enemy action, military power or rebellion.

The following classes of property are excluded from the cover given by an ordinary fire policy unless they are specifically mentioned and insured against:— Goods held in trust or on commission, money, securities, stamps, documents, manuscripts, business books, patterns, models, moulds, plans, designs and explosives.

Loss of Profits. A policy of fire insurance enables a manufacturer whose works have been destroyed by fire to reconstruct his buildings, install new machinery, obtain fresh supplies of raw material, and start business again with a factory as well equipped as that burned down. In like manner a shopkeeper, a warehouseman, or other trader recovers under his fire insurance policy a sum sufficient to put himself in as good a position after the fire as he occupied immediately before it. In other words, he has been indemnified against his material loss, assuming, of course, in every case that his insurance was for an adequate amount and that he has complied with the conditions of the contract. During the period of negotiation for the settlement of the loss and reinstatement of his premises, however, he will have become acutely aware that the material loss is not his whole loss, and that, unless his fire policy has been supplemented by a consequential loss policy (sometimes called a "loss of profits" policy) he is still seriously out of pocket.

Interruption of Output. For the sake of convenience the case of a manufacturer may be considered, but in varying degree the conditions are the same for a merchant or shopkeeper. The amount of the loss may possibly be settled with the insurance company in the course of a few days, but if the premises were extensive and the loss has done much damage, it will probably be several weeks before he can formulate his full claim, and further time must necessarily elapse before the items can be checked and agreed by the insurance company's assessor, salvage (if any) be realized, and a settlement reached. During all this time manufacture will have been at a standstill or if carried on in temporary premises, the work done under such conditions that the output has been greatly reduced and cost of production per unit increased. Orders, consequently, will have been delayed or have remained entirely unfulfilled. The next thing is that the manufacturer will hear that his customers, often without giving him a chance of showing what he can do, are going to his competitors, and he will know full well that it will be difficult to get them all back again. Some will almost certainly not return. He will also find, as he is not able to give employment and cannot afford to pay wages for nothing, that skilled hands gradually drift to rival firms.

Standing Charges. These troubles, however, are not all. Although he is not manufacturing, some of his expenses will still run on. Among them are interest on debentures, mortgages, loans and bank overdrafts; rent (sometimes); certain rates and taxes; directors' and auditors' fees, and many others.

Assignment of a Fire Policy. A fire insurance policy cannot be assigned without the consent of the insurer, because it is a personal contract. Therefore the benefit of insurance does not pass to the buyer with the sale of property which is covered by fire insurance. But policies generally contain a provision with regard to assignment.

In India section 49 and 135 of the Transfer of Property Act are applicable to the assignment of fire policies. Section 49 defines the rights of the transferee of immovable property insured against fire, while section 135 states the right possessed by the assignee of a fire or marine policy. These sections read as follows :—

Section 49 Where immovable property is transferred for consideration, and such property or any part thereof is at the time of transfer insured against loss or damage by fire, the transferee, in case of such loss or damage, may in the absence of a contract to the contrary, require any money, which the transferor actually receives under the policy, or so much thereof as may be necessary to be applied in reinstating the property.

Section 135. Every assignee, by endorsement or other writing, of a policy of marine insurance or a policy of insurance against fire in whom the property in the subject insured shall be absolutely vested at the date of the assignment, shall have transferred and vested in him all rights of suits, as if the contract contained in the policy had been made with himself.

Settlement of Claim It is the duty of the insured to understand thoroughly the terms of the policy, otherwise he may find that he has lost the benefit of the insurance owing to his not observing the conditions of the contract. For instance it is stipulated that whenever a loss by fire occurs, immediate notice shall be given to the insurance company, and full particulars of the claim lodged within a certain period. Therefore in the absence of proper notice no claim for compensation can be made.

Immediately after the fire, therefore, a written notice should be sent to the insurance company, and on the occurrence of a fire it is also the duty of the insured to adopt every available effective means for its extinction. On receipt of the notice the company will supply to the insured a claim form. This should be carefully filled in, giving full details of the property damaged or destroyed and an estimate of loss. All claims are to be supported by such vouchers, proofs and explanations as may be requested by the insurer.

In order that no bogus claim be paid the insurance company has the right to investigate thoroughly into the origin of the fire, the condition of the building, the value of the property destroyed and all other matters which can in any way affect its liability. The actual loss sustained can be ascertained only by careful enquiry. If the amount of the claim is small, it will usually be settled by the company itself through its representative. But in case of bigger claims expert valuers, called assessors or surveyors are appointed for the purpose. A surveyor assesses the value of the property damaged or

destroyed, arranges for the disposal of the salvage in the best possible manner and does his best to settle the claim amicably with the insured. If the parties cannot agree as to the amount of the loss, recourse may be had to arbitration or the insurer may agree to reinstate the property. If the property destroyed has been insured with two or more companies, the company having the largest share of insurance will take up the settlement in hand for the other companies.

When there are more than one firm in respect of the same insured property, the company is not bound to pay in all more than the amount of the policy, unless after the loss or damage by the first fire it is reinstated to the full amount by paying a fresh premium. For example, if the total amount of the policy is Rs. 6,000 and if Rs. 2,500 has been paid as damage on the first fire, then in the case of the total loss on the second fire the company will not pay more than Rs. 3,500 irrespective of the amount of loss.

In case there exists more than one policy on the same risk, every company is liable to pay only its rateable proportion of the loss or damage to the property insured against fire, whether the insurance has been effected by the insured or any other person. If any of the policies is subject to average, then all the policies will be automatically subject to average.

Marine Insurance

The manifold risks, to which goods are exposed during their transport by land or sea, have brought into existence a system of transport insurance which consists of *marine insurance*, *railway insurance*, and *postal insurance*. The last two are not very largely used by businessmen, except in the case of goods which are valuable or which are likely to be damaged in transit.

But as far as carriage by sea is concerned it is essential that a prudent man should always insure his goods. Goods sent by sea are subject to far more risks than those carried over land and according to the contract of carriage—Bill of Lading or Charter Party—the shipowner is not liable for all risks. A B/L or a C/P always contains a clause which is called the "excepted perils clause." This clause mentions the risks such as Acts of God, the King's enemies, arrest and restraint by rulers, princes and people, fire, barratry of the master or crew, gales, standing and other dangers of navigation, for which the shipowner is not responsible. Hence it is to provide against loss caused by any of these excepted perils that marine insurance is necessary. Briefly it may be said with regard to insured goods that where the liability of the shipowner ends, that of the insurance company begins, and the two never overlap.

Marine insurance is an arrangement by which one party agrees to compensate the owner of a ship or cargo for complete or partial loss at sea. Among the subject-matters of marine insurance are the ship, cargo and freight. The rates of premium vary for the different markets according to the risk involved. For instance some markets are served by a first class line of steamers, and this fact has an important bearing on the question of the premium, as the risk of the goods being damaged or lost in such cases is not so great in comparison

with remote countries to which goods have to be shipped in inferior steamers.

Insurable Interest. In order to make the contract of insurance valid, the insured must have an insurable interest in the subject-matter insured. He must be interested in the property at the time of loss, though he need not have any interest at the time when insurance is effected. The following are examples of persons who have an insurable interest :—

- (1) Shipowners and owners of goods.
- (2) A mortgagee to the extent of the sum due to him.
- (3) An insurer who may re-insure to the extent of his liability.
- (4) The person entitled to receive freight.
- (5) The master and crew for their wages.
- (6) A trustee or bailee as regards property entrusted to his care.

When goods have been sold, the insurance policy on them is not transferred with the sale unless such transfer is expressed or implied in the deed of sale. The seller in such a case loses his insurable interest in the subject-matter of insurance as soon as the sale is effected.

How to Insure. Before an insurance policy is taken out, it is usual to get two or three companies to quote their lowest rates so that they can be compared. A special form containing the insurance proposal is filled in and handed to the insurance company either direct or through an insurance broker. This proposal must contain the date, the name of the person desirous of effecting the insurance, the name of the ship, the voyage, the description of the goods (i. e., the marks, numbers and contents of the packages), the mode of packing and the amount of insurance. As regards the fixing of the amount, insurance in excess of the value of the goods is not admissible. In estimating the amount to be insured it is the general custom to add to the cost of the goods the freight and expenses and also about 10% for anticipated profit.

On receipt of this proposal and the payment of the premium the insurance company makes out the policy and delivers it to the insured.

Lloyd's In India marine insurance business is carried on mainly by joint-stock companies, but in London this business is divided amongst insurance companies and a separate organization called 'Lloyd's'. There is a good deal of business rivalry between them. Lloyd's is an association of underwriters (insurers) who carry on business over the London Royal Exchange. The term "underwriters" arises from the fact that the persons, who signify their willingness to take part in the risk as insurers, subscribe their names to the policy and state the sum for which they respectively agree to be liable. By this means the whole risk is insured by a number of people. Insurance on the Lloyd's is effected through a broker, who on receiving instructions writes out the details briefly on a 'slip' and submits it to an underwriter who quotes a premium for the risk. If this quotation is accepted the underwriter initials the slip and inserts the amount underwritten by him. The broker then presents it in turn to other underwriters until the whole amount is covered. The

liability of the underwriters will be according to the amount subscribed by each. The insurance policy is then made out from the slip. It is signed by the underwriters concerned, and is handed by the broker to the insured on payment of the premium. *The broker gets his commission from the underwriters.*

Kinds of Policies There are several kinds of marine insurance policies.

A **Voyage Policy** is one taken out for a particular voyage, e.g., Bombay to Liverpool. The clauses in the policy define the *actual time* at which the insurer's liability begins and ends. This kind of policy is suitable for insurance on cargo and not on ship.

A **Time Policy** is one by which insurance is effected, not for a voyage, but for a specified period which should not exceed twelve months.

A **Mixed Policy** is so called because it covers insurance from and to certain places for a specified period, so that the policy is both a voyage policy and a time policy.

A **Valued Policy** is one in which the value of the property insured is expressly declared. The insurance company undertakes to pay the stated amount in case of total loss, or to accept it as the basis of assessment in the event of a partial loss. In case of the insurance of goods the agreed value usually includes cost of the goods, freight and shipping charges and a 10 or 15% margin for anticipated profit. This is the commonest form of a marine insurance policy.

An **Unvalued Policy** is one which does not state the value of the subject-matter of insurance. Therefore in case of loss or damage, the amount for which the insurer is liable would be found out by assessment, subject to the limit of the sum insured. In this case, if it is the goods that are insured, the value is to be taken at their cost plus shipping charges. This will not cover the prospective profit though in a valued policy the anticipated profit can be included.

A **Floating Policy** (also called '*open policy*') is a form of unvalued policy taken out for a round sum and the shipments made under the policy by various vessels are declared afterwards as they occur. Such a policy is intended to cover a series of shipments between two or more ports, and is usually taken out by merchants having a more or less continuous flow of shipments between certain ports. The advantages to be derived are that the assured obtains a *lower premium rate* and is *relieved of the trouble of taking out a new insurance policy for every shipment*.

A **Wager Policy** is one in which the insured has no insurable interest. Such a policy is of no legal effect, but an insurer who has agreed to become a party to it would not generally fail out of honour to meet his obligation under it, provided the true nature of the transaction has been explained to him. The common name for a wager policy is a '*P. P. I.*' policy (policy proof of interest or without further proof of interest than the policy itself).

The Policy. The marine insurance policy is a stamped document setting

forth the conditions on which the insurance is undertaken by the insurer. It is a complex document which is not easy to understand. The main clauses of a marine policy are as follows :—

(1) *Name of the insured.* This clause, in addition to the name of the insured, makes provision for the assignment of the policy so that a person who subsequently acquires interest in the subject-matter may avail himself of the protection given by the policy.

(2) *Lost or not lost.* Sometimes insurance is effected on ships or goods which are on the sea, and both the insurer and the insured are ignorant of the safety or otherwise of the subject-matter of insurance at the time of effecting insurance. This clause has a retrospective effect and provides that the insurer would indemnify the insured in the event of the property being lost even though it might be discovered that the loss had occurred before insurance was effected. On the other hand, if the insurer knows at the time of the entering into the contract that the subject-matter has safely arrived, he will have to return the premium because there is no risk to undertake.

(3) *Description of the voyage.* "At and from." It must be noted that there is a difference between an insurance "from a port," and an insurance "at and from a port." The former means that the risk begins after the ship has left that port, while the latter indicates that it begins while the ship is at the port and after she has left the port. These terms are used in voyage policies. But in time policies the exact hour and date of the commencement and termination of the risk are stated.

(4) *Name of the vessel.* The vessel can be changed only with the consent of the insurer except when disaster to the ship named makes transhipment necessary.

(5) *Commencement and duration of risk.* In this clause an accurate description of the commencement and termination of risk is given. Where goods are insured "from the loading thereof," the risk will not attach until the goods are on board, and if the risk continues until the goods are "safely landed," they must be landed in the usual manner and within a reasonable time at the port of destination otherwise the risk continues.

(6) *Touch and stay.* It is essential that an exact description of the voyage should be given in the policy, because it is assumed by the insurer that an ordinary course of the voyage will be pursued. This clause permits the vessel to call at the ports in the ordinary course of her voyage and in the ordinary geographical order. The call must be made for purposes of the voyage. When a ship deviates from the voyage contemplated by the policy without a lawful excuse, the insurer is discharged from liability. But the deviation of the ship from her usual course of navigation is legally excused in the cases mentioned below :—

- (a) If it has been authorised by the policy.
- (b) Where it is caused by circumstances beyond the control of the master and his employees, e. g., the ship being blown out of her course by violent gales.
- (c) Where necessary for complying with a warranty, express or implied e. g., putting into a port for repairs in order to make it sea-worthy.
- (d) For the safety of the ship or cargo.
- (e) To save human life or to obtain medical help.
- (f) If deviation is caused by the barratry of the master or crew, if barratry be one of the perils insured against.

Where deviation is allowed, the insurance stands good and the insurer is not discharged from liability.

(7) *Valuation*. This clause states, in the case of a valued policy, the value of the subject-matter as agreed upon for insurance. In an unvalued policy no amount is mentioned but the valuation is made at the time the claim arises.

(8) *Perils insured against*. This clause describes in full all the risks or perils covered by the insurance in connection with which the insurer undertakes to indemnify the insured. The risks insured against are :— (a) Perils of the sea, e. g., damage by water, storms, collision, stranding, (b) Fire, (c) Pirates, rovers; (d) Thieves; (e) Jettison; (f) Arrests, restraints and detentions of all kinds; and (g) Barratry of the master and crew.

In times of war if the insurer does not want to undertake the risk of capture and seizure there is a special clause called "F. C. S." (Free of Capture and Seizure) is inserted in the policy which relieves the insurer from liability on account of this risk.

(9) *Sue and labour*. By this clause the insurer gives to the insured the necessary power to take all necessary steps to safeguard the subject-matter insured. The insurer further agrees to pay to the insured any reasonable expenses incurred by him in avorting or minimising a loss covered by the policy.

(10) *Waiver*. This clause provides that in case of accident, either the insurer or the insured may take such steps or incur such expenses, as are contemplated under the sue and labour clause, in order to prevent loss *without prejudice* to his right under the policy.

(11) *Consideration*. The insurer acknowledges receipt of the premium which he has charged for the risk.

(12) *The memorandum*. The N. B. attached to the foot of the Lloyd's policy is known as the "memorandum". There are many commodities which are likely to be deteriorated much more than others owing to the effects of the perils insured against. Again there are commodities of a perishable nature in respect of which it is difficult to make the insurer liable. Hence to escape from a crop of small claims, the insurer makes use of this clause which provides that (1) on certain perishable commodities, such as corn, flour, fruit, salt, fish, etc., the insurer is not liable for partial loss at all; and (2) in case

of less perishable articles like tobacco, sugar, hides, skins, the insurer is not liable for partial loss unless the damage caused comes to at least 5 per cent of the value of the goods damaged. On other risks the insurer is not liable for losses below 3%. But in all cases he is liable for partial losses below the given percentages when it is a general average loss or the ship is stranded, burnt or sunk. By stranding we mean that a ship sticks to the ground and does not move. Mere touching the ground shall not be taken as stranding of the ship. General average loss is an extraordinary loss incurred in the interest of the whole enterprise. The effect of the memorandum clause is to free the insurer from particular average losses (explained later on) wholly in the first case and partially in the two subsequent cases. He is able to calculate his risk more accurately and quote lower rates of premia.

In addition to the foregoing, there are other special clauses which are found in some policies. The most important of them are:—

F. P. A. (Free of Particular Average). This means that the insurer is not liable for a partial loss of the subject-matter, other than a loss incurred by a general average sacrifice.

F. C. S. (Free of Capture and Seizure). By this clause risks of capture, seizure and detention are generally excluded from the policy in times of war; but if an additional premium is paid to cover "war risks" this clause will not be inserted.

W. P. A. (With Particular Average). This means that the insurer is liable for a partial loss as well.

A. A. R. (Against All Risks). This indicates that the policy covers all risks against which it is necessary to insure.

F. A. A. (Free of All Average). This means that the insurer is not liable for either general or particular average, but he is liable for total loss only.

F. G. A. (Foreign General Average). The general average statements are prepared in accordance with the law of the port of destination or the law of the intermediate port, if the voyage be broken up. The insertion of this clause means that it is arranged between the insurer and the insured that in the event of a general average claim arising under the policy the average statement made in a foreign country according to the law of that country shall be taken as the basis of settlement.

R. D. A. (Running Down Clause). This clause means an arrangement between the parties to the insurance that, if the vessel collides with any other ship and is found by a court of law to be the wrong doer, the underwriters will bear a part of the sum which the owners of the vessel are compelled to pay for damages. This clause applies to the insurance of ships.

Continuation Clause. It is possible that a time policy covering a ship may expire before she has reached the port of destination. It is, therefore, sometimes provided by means of this clause that in such a case "she shall, provided previous notice be given to the insurer, be held covered at a *pro rata*

monthly premium to her port of destination.

Re-insurance Clause. Sometimes an insurer may undertake a risk much greater than what he considers safe to retain. He may re-insure with another insurer the whole or a part of the risk as he thinks necessary. A clause is then inserted in the policy explaining that it is re-insured subject to the same clauses and conditions as in the original policy.

Warranties. A warranty is a promise on the part of the insured that a particular thing shall or shall not be done in connection with the contract of insurance. The breach of a warranty in marine insurance would make the contract void and discharge the insurer from liability as from the date of breach. It may also be pointed out that the breach of warranty in other contracts does not render them void but only gives right to claim damages from the party responsible for the breach. Warranties found in a marine policy may be express or implied.

An express warranty is one which is incorporated in the policy. The following are examples of express warranties :—

Warranty to sail on or before a certain date.

Warranty prohibiting navigation within certain limits.

Warranty as to the neutrality of ship and cargo.

Two good examples of express warranties already mentioned are the F. C. S. clause and the memorandum.

An implied warranty is not stated in the policy, but every policy is deemed to contain the following three implied warranties :—

(1) *Sea worthiness.* A ship is sea-worthy when she is in a fit condition as to repairs, equipment, crew, etc., to encounter the ordinary perils of the voyage. She must be in a state of sea-worthiness not only at the port of start but at every subsequent port which she touches and stays at.

(2) *Non-deviation.*

(3) *Legality of the venture.*

Assignment of the Policy. A marine insurance policy can be assigned by the insured to any other person unless it contains terms prohibiting assignment. The assignment may be made by an endorsement on the policy. A marine policy is generally assigned by the insured to a person to whom he has sold the goods or to the agent to whom the goods are shipped. The assignee is entitled to sue on the policy in his own name, and in case of assignment notice to the insurer is not necessary.

In India the assignment of marine insurance policies is governed by section 135 of the Transfer of Property Act. This section contains the same provision as stated above.

Marine Losses

Causa proxima. An insurer is not liable for any loss caused by the wilful misconduct of the insured; but except where otherwise agreed to he is liable for any loss proximately caused by a peril insured against even though

the loss may be due to the negligence or misconduct of the master or crew. It is an important principle of a marine insurance contract that in order to make the insurance company liable for a loss such a loss must have been proximately caused by a peril insured against. The rule that the loss must be traced to a "proximate cause" has always been vigorously applied in insurance cases. Where a loss has been brought by several causes in succession to each other, some of which are insured against whilst others are not the proximate or the nearest cause of the loss must be taken into account; and if this is one of the perils insured against, the insurer would be liable otherwise not. For example, if some goods are insured against sea-risks, the insurer is not liable for a loss caused by rats. But if the rats cut a hole in the bottom of the ship, in consequence of which the sea-water poured into the hold and damaged the cargo, the nearest cause of the loss would be sea-water, and the insurer would be liable. Take the opposite case. Suppose a shipment of mangoes is insured against loss through agrounding of the vessel. The vessel is agrounded and the mangoes are reloaded in another vessel, for which much handling becomes necessary, as a result of which the mangoes are found at the destination to be materially damaged. Now handling and reloading which are the proximate cause of the damage are not the perils insured against, hence underwriters are not liable to pay for the damage, though this handling and loading would not have been necessary but for agrounding—which was the distant cause of the loss. Marine losses may be *total* or *average*.

Total Loss A total loss may be *actual* or *constructive*.

Actual total loss occurs (a) when the thing insured is totally destroyed, as in the case of a ship sinking or cargo being absolutely destroyed by fire, (b) where the matter insured is still in existence but has entirely changed its nature, e.g. sugar dissolved by sea-water, or (c) where the insured is irretrievably deprived of it, as when his ship or goods have fallen into the hands of pirates.

Constructive total loss arises when the subject-matter of insurance though not actually lost is reasonably abandoned, when its actual total loss is unavoidable, or when it is damaged to such an extent that the cost of recovering or repairing it equals or exceeds its repaired value. In such a case no reasonable man will incur the required expenditure but will treat the goods as finally lost. Such losses are treated as equivalent to actual total losses and are accordingly indemnified by the underwriters. Suppose a ship strikes a rock and is considerably damaged. If the expenses in getting it ashore and repairing it equal or exceed the repaired value of the ship, it is an example of a constructive total loss on the ship.

Notice of abandonment is necessary in case of constructive total loss. All claims in the goods insured are abandoned in favour of the insurer who is entitled to do anything he likes with these goods after acceptance of the notice. Notice of abandonment must be given as soon as the insured is in the possession

of sufficient information about the details of the casualties, to entitle him to claim a total loss. In the absence of a notice of abandonment the insured can claim only a partial loss. Where the insurer has reinsured the goods no notice of abandonment need be given by him to the reinsurer. But the insurer is not bound to accept the notice of abandonment, in which case, the insured shall have to sue him in the court.

The amount of indemnity for total loss to be paid by the insurance company is arrived at according to whether the policy is valued or unvalued. In a valued policy it is the *insured value*, i.e., the sum named in the policy; while in an unvalued policy it is the *insurable value* of the property lost, that is, the prime cost plus expenses.

Average. The word 'average' as applied to marine insurance does not denote the same thing as in arithmetic. In marine insurance it means damage or loss sustained at sea. Average may be *particular* or *general*.

Particular Average. A particular average loss is a partial loss of the subject-matter insured, caused by a peril insured against and not being a general average loss. Such losses include those which arise from unavoidable causes such as storms at sea, fire, or accident of any kind including collision with other ships, running ashore, springing a leak, etc. Such losses are borne by the owners of the property or their insurers. In this connection the effect of the Memorandum and the F. P. A. clauses must be clearly understood. The former provides that the insurer is not liable for partial loss in case of certain goods and is not liable for a partial loss below a certain percentage in case of others. While the F. P. A. clause altogether relieves the insurer of liability on account of partial loss. In such a case the partial loss must be borne by the owner even though the goods are insured.

Measure of Indemnity and Statement of Particular Average. The measure of loss is the difference between the amount realized for the goods concerned in their damaged condition, and the sum they would have realized had they arrived sound. In case of an unvalued policy it is this amount that can be recovered from the insurance company subject to the limit of the sum insured. But in case of a valued policy, the amount so arrived at will have to be adjusted on the basis of the amount insured. In addition the insured can recover from the insurer any particular expenses incurred in preserving the thing insured and also extra charges necessary when goods arrive damaged, such as survey fees, salo charges, etc.

As soon as the goods are landed in a damaged condition from the ship, they are surveyed by an expert and disinterested surveyor who certifies as to their damaged condition and gives the cause for it as far as it can be ascertained.

Particular Average on Ship. The underwriters' liability is to pay the cost of repairs (not exceeding the insured value) incurred by the insured which must be reasonable and the repairs being prudently effected. The insured value

here has nothing to do with the settlement of claims. The insured value simply sets a limit beyond which insurance company is not liable to pay.

Particular Average on Freight. Freight is not capable of sustaining physical deterioration in the same way as ship or cargo. It cannot depreciate in value. So the particular average on freight must be a partial loss of it. When the freight is paid in advance the shipowner has no risk to cover, but the shipper has. The underwriters are liable for the actual loss of the freight sustained by the insured. For example a cargo of salt is shipped, the freight being payable at the port of destination and during the voyage half of the salt dissolves owing to a peril insured against. One half of the freight is lost. The underwriters in this case would be liable for one-half of the amount of freight insured subject to the terms of the policy.

General Average. A general average is a loss caused directly by a general average act, and there is a general average act when any extraordinary sacrifice or expenditure is voluntarily and reasonably made or incurred in time of peril for the purpose of preserving the property imperilled in the common adventure. Whenever a general average loss occurs the party on whom it falls is entitled to a rateable contribution from the other parties in the adventure, and such a contribution is called general average contribution.

The essential features of a general average contribution are:—(1) The common adventure must be in danger, (2) There must be a necessity for sacrifice; (3) The sacrifice must be voluntary, i. e. intentional on the part of the man and not accidental, (4) It must be reasonably and prudently made; (5) It must be extraordinary in nature and must be made with the object of securing the common safety of ship and cargo, (6) There must be preservation of the ship and some portion of the cargo, (7) The common danger must not arise through any default on the part of the person whose interest has been sacrificed.

The losses giving rise to a general average contribution are of two kinds:—(1) Sacrifice of property, e. g. jettison (throwing cargo overboard to lighten a ship), destroying any part of the ship, damage to the cargo by pouring water over it to put down a fire or the burning of cargo as fuel for the engines; (2) Extraordinary expenditure properly incurred in time of peril for the preservation of common adventure.

Contributing interests The interests for whose benefit a general average loss is incurred are the owners of the ship and cargo and the receiver of freight. Therefore these three interests are required to make a general average contribution. The owner of the ship contributes to G/A on the value of the ship in the condition in which she arrives at the port of destination. The receiver of the freight contributes on the net amount of the freight saved by the sacrifice. The value of the cargo, as a contributor, is taken at what it would fetch if sold on arrival, after deducting all charges. Hence in dealing with general averages, the "contributing values for general average" determine

the proportion in which the loss is divided, and they are not always the same as the insured values. Thus the insured value of a cargo may be £1,000 but its market value at the port of destination may be £2,000 and it is the latter value on which the owner of the cargo will be required to make a G/A contribution.

Average Adjustment. When a ship arrives at a port, after the happening of the general average loss, it is necessary for the master of the vessel to appoint professional experts known as average adjusters to prepare the average statement showing the amount of the G/A contribution due. The master of the vessel must justify any course of action he has taken by making a declaration called *protest*. The declaration is to be made before a Notary Public and sets forth all the circumstances of the case as recorded in the ship's *log book*.

If the G/A loss has arisen from a peril insured against the shipowner and the merchants paying general average contributions are entitled to recover the amounts so paid from their insurers.

Salvage is the reward paid to a salvor for saving or helping to save property or property and life conjointly at sea. The word is also used to express the property saved. A salvor has a lien on the property he has saved as security for the reward of his services. He cannot legally recover any amount by way of salvage, if his efforts do not result in saving the property.

Bottomry. In early times when the facilities of communication were not satisfactory, masters of ships were sometimes forced by circumstances to borrow money on the security of the ship or ship, freight and cargo. Such contracts were made by bottomry bonds. The chief characteristics of a bottomry contract are (1) that the money is absolutely essential to prosecute the voyage, (2) that it cannot otherwise be raised except by a bottomry bond, and (3) that the amount borrowed is the minimum required for repairing the ship and prosecuting the voyage. The master pledges his personal credit as well, and thus becomes personally liable. It differs from an ordinary money lending against securities. There is the element of insurance, in as much as, if the ship is lost in the way and does not reach its destination, there is no claim on the bottomry bond. But the loss must be a total loss. In case of a partial loss the money borrowed shall have to be repaid. If the master of a ship is compelled to borrow on bottomry bonds at Aden, Malta and Gibraltar on his way from Bombay to London, the last lender (of Gibraltar) shall have the first claim and the first lender (of Aden) shall have the last claim for repayment of the respective amounts. It is based on the principle of necessity. If the last money lender would not have helped, the ship could not reach her destination.

Respondentia. When money is borrowed on the security of cargo alone it is done by means of a *respondentia bond*. But the master must not resort to such a measure so long as he can raise money on the security of the ship and he must also try as far as possible to take the assent of the cargo owners to

pledge their property. The cargo owner has to be indemnified by the ship owner, if his goods are seized by the money lender on a *respondentia*—bond. Nowadays such contracts are absolutely out of place.

Test Questions

1. What is Insurance? Describe briefly the different kinds of insurance commonly effected by business houses. (*Bombay B. Com. 1936*).

2. Do you prefer life assurance to other forms of investments? If so, why? How would you select a life insurance company if you wished to insure your life? (*Agra B. Com. 1911*).

3. Explain the principal types of life assurance policies ordinarily issued, and state briefly the advantages and disadvantages of each.

(*Agra B. Com. 1946*).

4. Explain the nature and characteristics of insurable interest in relation to life assurance. To what extent, if any, do you consider insurable interest exists in the following cases?—

(a) A creditor on the life of his debtor ;

(b) A Father on the life of his child ;

(c) An employee on the life of his employer .

(d) A husband on the life of his wife. (*Agra B. Com. 1947*).

5. State the essentials of a valid contract. Explain how and to what extent a contract of life assurance satisfies the above essentials. In what ways can a contract of life assurance be terminated? (*Agra B. Com. 1947*)

6. Describe the types of assurance that you would suggest as most suitable to meet the following requirements, stating how they are met in each case :—

(a) To provide for the education of a child ;

(b) To protect dependents in the event of an early death and meet the needs of the life assured in later years ,

(c) To make provision for payment of estate duties ;

(d) To replace capital which has to be withdrawn from a business in the event of the death of a partner .

(e) To provide a capital sum at a specified date.

(*Agra B. Com. 1947*).

7. Write short notes on (a) nomination on the face of a policy of life assurance , and (b) conditional and unconditional assignments.

(*Agra B. Com. 1948*).

8. How far can you judge the position of a life insurance company from the magnitude of its life insurance fund? If it is not a sufficient criterion, what means are adopted for the purpose? (*Agra M. Com. 1948*).

9. Enumerate the various documents usually called in by a life office for establishing a claim by death of the life assured, and discuss the importance of each of these documents. (*Agra B. Com. 1948*).

10. Explain the term 'General Insurance.' How do you account for the formation of a number of general insurance companies in India in recent years? What different risks should a prudent businessman cover by insurance?

(Agra B. Com. 1945).

11. Explain the principal types of fire insurance policies, and state the relative merits of each of them.

(Agra B. Com. 1948).

12. What are the principal implied warranties in the case of a marine insurance contract? Explain them clearly.

(Agra B. Com. 1947).

13. Explain clearly the following extract taken from the Directors' Report of a leading Bombay cotton mill company for the year ended 31st December, 1943 :—

'The Company's property including buildings, machinery, and stock has been insured for Rs. 1,26,00,350 and the profit and standing charges of the Company have been insured for Rs. 55,00,000 to cover a maximum stoppage of 24 months. The Company's mill buildings, machinery, and stock have been insured against war risk in accordance with the Ordinance of the Government of India.'

(Agra B. Com. 1945).

14. Discuss the role of insurance in modern Commerce.

(Rajputana B. Com. 1949).

CHAPTER 11

PRODUCE EXCHANGES

A commodity market may be defined as a permanent and organised place where persons meet for the purpose of doing business in a commodity which may be a natural product of the soil such as wheat, cotton, jute, linseed, tea, etc.; a mining product such as gold, silver, lead, copper, etc. or a manufactured article such as jute fabrics, cotton textiles, sugar, etc. The term 'Produce Exchange', on the other hand, is confined to a market for raw produce only, such as wheat, cotton, jute, linseed, gram, etc.

Only those commodities which are capable of being graded or otherwise accurately described and being sold in large quantities are suited for sale in an organised market. The essential characteristics of an organised market are a large number of competing buyers and sellers; a large quantity of the commodity dealt in; the organisation by which all persons interested in the commodity can quickly communicate with one another, the collection and frequent publication of statistical and other information relating to the present and the probable future supply of commodities, the actual buyers and sellers do not transact business in person but do it through brokers, and the demand and supply are concentrated.

One essential feature of an organised market is the quick dissemination of commercial news. This has been made possible by the development of rapid means of communication such as telegraph, telephone and wireless. The principal radio stations of the world broadcast commercial news every day. Every organised commodity market has a standard form of contract specifying the grade, and the conditions for payment, for delivery and for the settlement of disputes by arbitration. It has usually a futures clearing house, by means of which the purchases and sales of dealers can be offset and the settlement of contracts easily made.

Mandis or Wholesale Markets

A mandi is a wholesale market held in a fixed market place where business is transacted daily. In many of the old mandis the shops are arranged on both sides of a road, whereas modern mandis like those in the Canal Colonies of the Punjab and the Western United Provinces are invariably built in the form of a square or a quadrangle, each side having a gateway. As the produce is handled in fairly large quantities, specialised functionaries such as weighmen, brokers and commission agents operate in these markets for the performance of different services. Mandis serve as assembling points for the local produce and also as centres of distribution. Mandis in India are either centralised or decentralised. In a centralised mandi, 'arhatiyas' shops are all situated in a

particular locality, e.g., Meerut and Muzaffarnagar mandis. In the case of a decentralised market, shops and godowns of *arhaliyas* lie scattered in different parts of the town, and each of them serves as a market place. A typical example of this kind of market is the important potatoe market of Farrukhabad in the U. P.

Mandis are usually owned by private persons, local bodies (such as municipalities, district boards, notified areas, etc.) or by Government. In Assam, Bengal and Bihar the markets are mostly privately owned, but in the United Provinces more than 50 per cent. of the mandis are owned by municipal boards, about 25 per cent. by zamindars and private individuals, and the remainder by Government, Chambers of Commerce, Courts of Wards, etc.

The area served by wholesale markets depends largely upon communication and transportation facilities, the nature of commodities handled, location of the market with respect to other markets and the nature of market (that is, regulated or unregulated). If proper means of transportation are available, the commodity is durable, the market is favourably situated and properly regulated, it can serve long distances.

The various means of communication in India are roads, rail, inland waterways, sea, and postal, telegraph and telephone facilities. Road transport consists of head-loads, pack animals, carts and motor trucks. The method of carrying loads on head is employed mostly in case of vegetables and fruits and in hilly areas. Sometime the load is carried across a shoulder in a *bahangi*. Pack animals are commonly employed in tracts having poor roads. By far the commonest means of transporting produce from villages to the mandis is the bullock-cart. Motor trucks can operate only on pucca roads. The cost of conveyance depends upon the condition of road, distance, season, and the possibility of obtaining a load on the return journey. Motor truck is cheaper and quicker.

The chief sources of market intelligence available in urban areas are Government publications, trade papers, private arrangements and radio. Generally speaking, traders keep themselves well informed about the market conditions prevailing in different parts of the country.

The nature of commodities handled in different mandis varies according to the local surplus production on the one hand and the demand for commodities not grown in the locality on the other. For instance, in the mandis of the western U. P. surplus commodities such as wheat, sarson, gur, etc., form a large proportion of the total produce handled. On the other hand, rice, cotton seed, maize, etc., are imported from areas of surplus production. Arrivals of different commodities in a particular market fluctuate according to their harvesting seasons. The movement of produce appreciably slackens during monsoons due to the bad condition of kachcha roads and also the possibility of the produce getting spoiled in transit.

The question of the storage of agricultural produce in the mandis is very

important, because a fairly large proportion of crops find its way there within a short period of the harvesting season and awaits distribution sometimes for considerable periods. Generally speaking, most of the non-perishable agricultural commodities are stored in kuthas, godowns, and khattis. Khattis are either kachecha or pucca. In Muzaffarnagar, for instance, there are cement lined khattis.

The assembling and distribution of agricultural produce in wholesale markets are financed by the following agencies:—Kachecha and pucca arhatiyas, money-lenders, banks, grain trade associations and exporters. The various agencies advance loans on the security of standing crops, value of produce, hundis and also on personal security. Hundis play an important part in this connection.

Most of the mandis are not subject to any statutory control, and the business is conducted according to market practices established by custom. In some mandis arhatiyas have established panchayats to manage their affairs. A few regulated markets have been established by Provincial legislation in certain provinces. They are managed and controlled by committees on which the producers are also represented. The various persons functioning in a mandi are arhatiyas, dalals, palledars, etc. The kachecha and pucca arhatiyas play an important part in the assembly and distribution of produce. The dalal assists the arhatiya in bringing together sellers and buyers and arranging the sale of produce. Telas, palledars, water men, munnas, etc., are also important constituents of the mandi.

Arrived at the mandi the produce is taken to the shop of an arhatiya with whom the seller has his dealings. Sales are effected by arhatiyas through dalals. When the price has been settled, the produce is weighed and bagged by the market functionaries concerned and sent to the buyer's godown. The basis of sale varies with different commodities. Wheat and other grains, for example, may be sold either on clean basis or subject to karda (refraction). Samples of produce are analysed, and the quality is then agreed upon. There is lack of uniformity in drawing samples and in analysing them. Weights and measures are not the same throughout India, and their standardisation is essential for improved marketing. Weighment is done either by hand scales or by hanging scales.

Market charges levied go under a variety of names in different mandis, but generally speaking they include akrit, dalal, palledar, tulai, and dharmada. An allowance for karda is made before calculating the price of the produce sold. Some of the charges are unwarranted and are an unjust burden on the seller.

Produce Exchanges

A produce exchange may be regarded as a specialised wholesale market devoted to a particular commodity or a group of commodities, where trading is confined to members who may, however, transact business for non-members also. Business is done according to definite rules and regulations laid down in the

bye-laws of these institutions. The management is vested in a board of directors elected after fixed periods by the members. Although the main function of produce exchanges is to provide facilities for trading in "futures", some of them like the East India Cotton Association, Ltd., Bombay, regulate spot transactions also, while a few others like the Indian Produce Association, Calcutta, confine their activities to spot transactions only. The produce exchanges are linked with world markets through a quick agency of market news service and are thus able to secure a certain amount of parity of prices, which is an important function of an efficient and organised market. The produce is not exposed for sale except in the case of spot transactions where small samples may be employed to indicate the quality of the produce traded in. Business in "futures" is done on the basis of accepted grades. The turnover of the "futures" transactions is usually very large as compared with spot business. All the contracts are, however, not liquidated by the actual delivery of goods; the majority of them are settled by the payment of differences in the prices. In making payments, instruments of credit such as hundis are freely made use of. The business is usually done through brokers. The provision of facilities for arbitration in case of disputes is an important feature of the produce exchanges.

The majority of produce exchanges in India have been organised primarily for dealing in "futures", although some of them control spot trading as well. "Futures" is an abbreviation of the original term "contracts for the future delivery of cotton" first used in the United States of America. In course of time, however, the word has become wider in application and now covers dealings in futures contracts in various agricultural products and other commodities on organised exchanges run by associations of traders.

'Futures' contracts are a form of price insurance as may be illustrated by a simple example. Suppose the price of a particular commodity in the terminal market is Rs. 100. If a merchant thinks that he can profitably buy in up-country and deliver at that price, he proceeds to buy in the up-country market and at the same time sells on the 'futures' market an equivalent quantity at that price. By the time the goods eventually arrive, the price may have risen or fallen. Suppose the price falls to Rs. 85. The merchant sells his goods at that price suffering a loss (as against his expectation) of Rs. 15; but by liquidating his sale of an equivalent quantity on the 'futures' market he makes a profit of Rs. 15. Thus he is covered against the fall in price. Conversely, in the same set of circumstances, a manufacturer having contracted to sell his finished product when raw material is costing Rs. 100 insures or protects himself against a rise in his costs by buying 'futures' at that price. Should such a rise occur, he is at liberty to sell out his 'futures' contract and set the profit so made against the loss on the actual purchase of raw material.

The main feature in which a "futures" contract differs from a "spot" (or "ready") or "forward" contract is that whereas a spot contract is a contract for immediate delivery of goods and a forward contract for delivery of goods

at a future date, a futures contract (although having the stipulation like a forward contract for delivery of goods on a future date) may also be liquidated—as is more usual—by payment of difference at any time during the currency of the contract.

The growth of 'futures' trading in India is a comparatively recent development brought about mainly by the changed conditions arising from the War of 1914-18 and as a result also of the increasing importance of the internal market. Until a few years after the last War, the greater proportion of the export trade in grains and oilseeds and a considerable part of the cotton and jute export trade lay in the hands of a few large international firms. These concerns maintained widespread buying organisations upcountry and established direct contact with the producers. Large quantities of the saleable surpluses of various commodities were disposed of to these firms for cash to be immediately despatched to the ports and shipped abroad. The ramifications of this system appear to have had some effect in stabilizing or at least in co-ordinating prices in the different markets. During the last War, the normal channels of trade were disorganised and the prevailing uncertainties encouraged a wave of speculation which resulted in many difficulties, not the least of which were the numerous failures and defaults which took place. Since there were few markets in which organised 'futures' trading existed with rules and regulations for the proper conduct of business, legitimate traders were subjected to severe strains and handicaps. While the 'futures' trading in cotton and certain agricultural products had already been in existence at Bombay in some sort of organised form for a number of years prior to 1914, the first serious attempt towards organisation in any upcountry market seems to have come in 1920 when the now defunct Sugar and Grain Merchants' Association was formed at Amritsar in the Punjab. The lineal descendant of this body is the present Indian Exchange, Ltd., which is one of the more important institutions of its kind in India. In Calcutta, a small jute 'futures' trading association had been organised in 1912, but no jute was actually delivered and the market was used solely for gambling. After a somewhat chequered career it was finally closed down by the local authorities in 1926-27. Two other jute 'futures' associations were formed in 1926 but these also were suppressed in 1928 and 1929 respectively. The East India Jute Association was established in Calcutta in 1927 and now controls the jute 'futures' market in India. Bombay has probably larger experience of 'futures' trading than any other market in India. There were, for example, several associations of cotton trade interests in Bombay prior to 1914, two being concerned directly with the conduct of 'futures' trading. These were replaced by the East India Cotton Association constituted by statutory authority in 1922.

Although there have been no great changes in the number of 'futures' trading associations at the ports, a remarkable expansion in their activities took place throughout Northern India between 1920 and 1933. Their main business

lay in trading in wheat "futures" although provision for trading in other commodities such as gram, barley, rapeseed, etc., was also made in their rules and regulations, and a certain amount of business did take place in those crops. By 1934, however, many of these 'futures' associations had failed and more than half of their number was moribund owing to their financial instability and lack of experienced management. Serious irregularities such as the non-observance or relaxation of the rules were also responsible for the unsatisfactory state of affairs.

These produce exchanges are usually organised as follows :—

Constitution and management. The 'futures' trading associations or produce exchanges fall into two main classes, viz., (a) non-profit-sharing and (b) profit-sharing and are registered under the Indian Companies Act. Almost all the non-profit-sharing associations are located at the ports. The East India Cotton Association and the Marwari Chamber of Commerce, both of Bombay, and the Karachi Indian Merchants' Association may be cited as typical instances. The profit-sharing associations are found upcountry only. The Indian Exchange Ltd., Amritsar, is one of the most outstanding examples of this class. It is significant that the non-profit-sharing associations enjoy a greater degree of stability and influence than the majority of the profit-sharing associations. The former also provide their members with vastly greater amenities than those afforded by the associations in the latter category. The management of both classes of associations is vested in boards of directors or committees, the composition of which varies with the different institutions.

Methods of business. In most of the produce exchanges, business is transacted at odd places in the market square or in the street. Only a few exchanges possess trading halls or special premises for this purpose, these trading places being known as "pits" or "rings".

(a) **Brokers.** Brokers play a large and important part in the 'futures' markets. As a general rule, these functionaries are licensed by the respective associations and are required to deposit some form of security—personal or cash. The rules governing the appointment or recognition of brokers are, however, observed with considerable laxity at many places. In important towns having telephonic facilities, many brokers have telephones on their premises so that they may keep in touch with their clients. Less influential brokers keep moving about between the pit and their clients' shops informing the latter about the latest rates and trends and securing orders accordingly. During business hours, there is always a large number of brokers present in the "pit." The brokers shout their bids and offers at the top of their voices and use terms and gestures peculiar to the trade with the help of which they are able to conduct a large volume of business within a few minutes even amidst the din and clamour in the "pit."

(b) **Registration of contracts.** The system of registration followed by the majority of upcountry exchanges may be briefly described as follows.

After a transaction has been made, the brokers concerned enter it in their rough note books. Each certified broker is usually issued a book of printed forms by his association. These forms are generally in triplicate. From his rough note book the broker makes the necessary entries in the printed forms which are subsequently countersigned by the parties concerned. Then the seller's broker hands over one copy to the buyer's broker, one to the seller and retains the third for his own record. Similarly the buyer's broker gives one copy to the seller's broker, one copy to the buyer and keeps the third for himself. As a rule the members of a 'futures' trading association are required to send to the office of the association, by a certain specified time (varying in the case of different associations) each day, forms giving the list of their transactions on the previous day. These forms are generally known as "Position Forms" and are sent to the office of the exchange along with the broker's slips. Both are carefully checked in the association's office and, if found correct, the transactions are confirmed and registered.

(c) **Margin Money.** For every contract registered with an exchange a member is required to deposit a certain sum of money according to the rules of the exchange. This deposit is known as the margin money and serves as a security against any losses to the exchange on account of fluctuations in prices. The amount of margin money demanded varies appreciably in different exchanges. The rules of the majority of the associations specify that margin money must be deposited at the time of getting each transaction registered. Afterwards the position of each member is carefully watched and as soon as it is found that any member has less than a safe margin with the exchange, he is called upon to deposit more money to bring it up to the prescribed level.

(d) **Units of trading and months of delivery.** The units of trading vary considerably in different markets. 'Futures' contracts are generally made in respect of certain specific months, e. g., December, March, May, etc., and are known by the name of the month. Months of delivery in which 'futures' contracts are traded vary widely even in the same commodity in different markets.

(e) **Contract forms.** Futures transactions are further governed by certain other terms and conditions laid down in contract forms (in which each transaction has to be entered) adopted by the various exchanges. The most important of these relate to the basis of refraction in the produce tenderable and the scales of allowance in the event of refraction exceeding the free tolerance limits. The procedure of arbitration and charges leviable by the exchange are also laid down.

N.B. Trading on the 'futures' is generally confined to the members of an exchange. Non-members can, however, transact business through the members of the exchange by paying a certain amount of commission in addition to the charges levied by the exchange from its members. These outside members have

also to deposit margin money with their commission agents. In this manner business by traders in a market, which has no facilities for 'futures' trading, may be conducted in distant markets, having organised produce exchanges, through the medium of commission agents and other intermediaries.

Produce Exchange Terms

Ready Business. This is purchase and sale of goods for ready or spot delivery. Ready business is also known as *trading in actuals*. The supply of goods for the ready business comes from the existing stocks or accumulations held by merchants and from fresh arrivals. Agricultural produce reaches the market throughout the year, sometimes (particularly at the harvest time) in large quantities and sometimes in small. The demand for ready goods arises from the trade stockists, millers, jobbers, dealers, consumers and speculators.

Forward Business. Contracts for forward delivery are either *forward 'contracts'* or *'futures contracts'*. A forward contract is one whereby the delivery of goods is to be made at a future date, while a futures contract is one in which there is a stipulation, like a forward contract, for the delivery of goods at a future date, but which may also be liquidated, as is more usual, by the payment of difference at any time during its currency.

Futures are available in all important commodities and in all the principal markets. Futures are described by the name of the month in which delivery is due, and the months of delivery are different for different commodities and in different markets. In some markets the delivery months are calendar months and in others Samvat months. Where two or more futures of the same commodity are running at the same time in the same market, they are distinguished by the names of the delivery months or as near and distant positions according to the time of their delivery.

Speculation. Speculation takes place in futures; it cannot exist in ready business. If a person buys or sells a commodity for forward delivery and means to take or give delivery at the due date, such a transaction is a genuine trade transaction. But if a person buys or sells a future not with the object of taking or giving delivery, but for the purpose of settling it before the due date in order to make a profit on the transaction, such a dealing is speculation.

The term 'Speculation' is commonly looked down upon by the general public who regard it as pure gambling. But that is not quite true. Speculation is a science by which one attempts to make an intelligent forecast of the future course of prices of a certain commodity. The difference between speculation and gambling may be summed up in these words: "Speculation begins where foresight enters and gambling begins where foresight leaves." There is, of course, an element of chance in both speculation and gambling, and speculation is looked upon with contempt because it is risky. The consequences of rash speculation are very often disastrous. When there is too much speculation in any commodity, it is said to be *hectic, wild, frenzied* or *unbridled speculation*.

Speculation beyond one's means and based on rumours and not on adequate knowledge is *gambling*.

Speculators may be professionals or amateurs. A professional speculator is one who devotes his whole time and attention to this business and who studies closely all the available information on the subject. An amateur speculator, on the other hand, is a person who does speculation as a side job and who very often does not possess any information about the commodity in which he speculates. He simply goes on hearsay. Amateur speculators, with rare exceptions, invariably lose. Speculators are either bulls or bears.

Bulls. A speculator who *buys* forward with the object of selling again at a profit before the date of delivery is known as a *bull*, a *long* or a *bull operator*. The phrase '*to go long*' means to act as bull, that is, to buy a future in the hope that its price will rise. '*The long side of the market*' is another phrase commonly employed, which means purchases made by bulls.

Stale Bull. When the forecast of a bull goes wrong because the market falls instead of rising, and in spite of his waiting for a long period the prices do not move in his favour, then he is called a *stale bull*, a *tired bull* or a *disappointed bull*. If he cannot wait any more, he will have to unload at a loss.

Staunch Bull. He is a speculator who always acts as a bull, and never as a bear.

Bull Support. The word '*support*' in market language means to buy. Bull support simply means purchases made by bulls. *Bull activity* is another phrase used in the same sense.

Bull Factor. Any factor which is likely to raise the price of a commodity is known as a bull or bullish factor.

Bullish Outburst. Heavy purchases made by bulls in a rising market are referred to as bullish outburst.

Bullish Sentiment. An idea amongst speculators that prices will go up is known as bullish sentiment.

Bull Liquidation. Sales made by bulls in order to settle their previous commitments are termed as bull liquidation or unloading by bulls. To unload means to sell, particularly when one has to sell at a loss. A person has a sense of relief when he unloads a heavy burden from his head; similarly a bull selling his purchases at a loss is said to unload them.

Bull Account. When the speculative purchases of a certain commodity exceed its speculative sales, there is said to be a bull account or an overbought position in that commodity, or the technical position of that commodity is said to be bullish.

Bull Campaign or Bull-Rigging. When a big bull account or an overbought position exists in any commodity, and the bulls try to bring about an artificial rise in its price by circulating in the market bullish news about it such tactics on the part of the bulls are known as a bull campaign.

Bears. A speculator who *sells* forward in the hope that before the date of delivery he will be able to purchase at a lower rate and thus make a profit on the difference is called a *bear*, a *short* or a *bear operator*. The phrase '*to go short*' means to act as a bear, that is, to sell a future in the hope that its price will go down. '*The short side of the market*' means sales made by bears.

Bear Sale. A forward sale made by a bear who does not possess the goods at the time of selling but who hopes to buy them before the due date of delivery is called a *bear sale* or a *blank sale* or a *short sale*. In practice the question of giving delivery does not arise, because, the bears usually get out of their commitments before the due date of delivery, by purchasing the futures which they sold and thus squaring their transactions.

Bear Covering. A bear sells a future in the expectation of a fall in its price, so that he may purchase it again before the date of delivery in order to fulfil his promise. If his calculations go wrong, and the price begins to rise instead of falling, he will be compelled to start buying. Such a purchase made by a bear is known as 'bear covering', the general effect of which is a rise in prices.

Bear Factor. Any factor which is likely to bring prices down is called a bear or bearish factor.

Bear Sentiment. An idea amongst speculators that prices will go down is known as a bearish sentiment.

Bear Account. When the speculative sales of a certain commodity exceed its speculative purchases, there is said to be a bear account or an oversold position in that commodity, or the technical position of that commodity is said to be bearish. A bear account is called 'open' or 'uncovered' when bear speculators have sold what they do not possess and what they have not yet acquired by purchase. An open bear account suggests that bear covering will follow leading to a rise in prices.

Bear Raid. When there is a bear account in any commodity and the bears attempt to depress its price by spreading in the market bearish news about it, such an action on the part of bears is called '*bear raid*' or '*bear tactics*'.

Bear Squeeze. Sometimes the heavy sales of a certain commodity made by bears pass into the hands of persons who know that there is a bear account in that commodity. The latter, therefore, secure as much supply as they can, and then demand a very high price before the settlement period. The bears under such circumstances are forced to cover themselves at whatever price they can, otherwise they cannot give delivery on the date. Whenever the bears are landed in such a difficult position, there is said to be a '*bear squeeze*' or simply a '*squeeze*'.

Tenders. The quantity of a certain commodity offered to be delivered by the bears on account of their forward sales is known as '*tender*,' and the goods which are available in a market for the purpose of being delivered in respect of forward contracts are called '*tenderable stock*'.

Note—Bulls and bears are speculators, they are also called market operators. A sort of a tug-of-war (known as a *speculative bout*) goes on between bulls and bears. In a rising market the bulls have the upper hand, but when prices begin to fall the market is seized by the bears. The majority of professional speculators are bears, while amateurs, being largely optimists, usually act as bulls. Both bulls and bears use their own tactics in order to bring round the market in their favour.

Options. An option is a right to buy or sell certain goods within a fixed time at a price settled at the time the option is given. The giver or seller of an option (called **option dealer**) receives from the purchaser of the option a fixed amount by way of premium (known as **option money**). If the price fluctuates in such a way as to make it profitable for the option holder to exercise it he will do so, if not, he will simply lose the money he paid for the option. The method of speculating by means of purchasing an option limits the amount of loss to the amount paid as option money.

There are two kinds of single option—the call option and the put option. The '**call option**' gives the right to buy or not, at the choice of the option holder, at an agreed future date a certain commodity at an agreed price, which is known as the '**striking price**'. The '**put option**' gives the right to sell or not, at the choice of the option holder, at an agreed future date a certain commodity at an agreed price.

There is also the double option ('**put and call option**'), which gives the right either to buy or to sell, at the choice of the option holder, a certain commodity at an agreed future date and at an agreed price.

In Indian market language option dealings are known as '**Teji Mendi transactions**'. '**Teji option**' is the equivalent of call option, and to buy a Teji option is known as '**Teji lagana**'. '**Mandi option**' is the same thing as a put option, and to buy a mandi option is '**Mandi lagana**'. The double option is known as '**Najrana option**', and to purchase a najrana option is called '**Najrana lagana**'. The person who buys an option is called '**Teji, Mandi or Najrana laganevala**', while the option dealer is known as '**Teji, Mandi or Najrana khanevala**'.

The price of an option, i.e., Teji, Mandi or Najrana rates, depends mainly upon market fluctuations, and are quoted daily along with the prices of futures. For amateur speculators the system of options is very useful, because by means of options they can limit their losses.

Take an example. Suppose on 19th April 1941 the rate of Jeth wheat futuro is Rs 3-2-6, the rate of Jeth teji option Re 0-1-3, the rate of Jeth mandi option Re. 0 1-4½, and the rate of Jeth najrana Re 0-2-6 per maund. If a person purchases on that date 100 maunds of Jeth wheat at Rs 3-2-6, he may make a good profit or sustain a heavy loss on this deal. If the price goes up to Rs 3 8 0 by the end of Jeth he makes a profit of Re 0 5 6 per maund, but if the rate of Jeth wheat drops down to Rs 2-12-0 he will incur a loss of Re. 0 6-6 per maund.

If, however, he wishes to limit the amount of loss, he should not buy 100 maunds of Jeth wheat future. He should instead apply najrana of Rs. 0.2.6 per maund on 100 maunds by paying Rs. 15-10-0. If he applies najrana, it means that by paying the sum he has secured the right either to purchase or to sell 100 maunds of wheat at Rs. 3.2.6 up to the end of Jeth, the actual date for the settlement of option dealings being Jeth Sudi 9 which is known as the **declaration date**. Whatever may be the fluctuations in the Jeth wheat rates, his maximum loss is limited to what he has paid by way of najrana; and of course, the greater the fluctuation either way, the greater will be the amount of his profit. If the price of Jeth future remains absolutely unchanged at Rs. 3.2.6 from the date of his purchasing the najrana option up to the najrana declaration day (that is, Jeth Sudi 9)—and this is highly improbable—then he would lose Rs. 15-10-0 altogether.

Protected Bear and Bull. If the buyer of teji option on any sharp rise in the market sells forward for the same month as that for which he has applied teji, he becomes what may be called a '**protected bear**'. Should the market fall back, he can repurchase for the same option month, and thus make a profit while retaining his option. The holder of a mandi option can also employ the same device in the reverse direction, that is to say, he can buy forward on a fall and become a '**protected bull**'; and if the market rises before his option expires he can sell for the same option month, secure a profit and still retain his option. This procedure is known as "**Teji ke pete bechna or mandi ke pete lena**". Skillful operators in actively fluctuating markets deal against options in this manner several times during the run of the option. Where the profits thus secured exceed the option money paid, the purchaser of the option has a profit and his option, so to say, for nothing.

Gale Option. When a person secures an option to buy or sell a certain commodity at a price higher or lower than that ruling on the day on which the option is purchased, such an option is known as a '**gale option**'. For example, if the price of Jeth wheat on a certain day is Rs. 3.2.6, and the rate of teji option for Jeth on that day is Rs. 0.1.7½ per maund, a person may apply gale option at Rs. 3.6.0 per maund instead of at the current rate of Rs. 3.2.6, for the rate of a gale option must be cheaper, say, perhaps only 6 pies per maund, because the risk undertaken by the option dealer is thereby considerably reduced. These speculators, who cannot afford to apply teji, mandi or najrana at the current commodity rates, purchase gale options.

Streddling. This is another protective method of speculation on the difference in prices of different futures of a commodity in the same market or difference in prices of the same future in different markets. Such a difference is also known as '**gap**', '**spread**', '**premium**', '**discount**' or '**satta**'. For example, if the price of Jeth wheat futures in Hapur is Rs. 3.2.6 and that of May wheat future in Bombay is Rs. 4.4.6 on a certain day, there is a gap or difference of Rs. 1.2.0 in the prices of the same future in two different

markets. If a speculator has reason to believe that this difference of Rs. 1.2.0 is more than usual (taking the cost of transportation into account) and that is likely to become less in future, he may sell in the Bombay market and buy in Hapur about the same quantity of May or Jeth wheat, in the hope that the gap will become narrow and thereby he will be able to make a profit on the deal. This form of speculation is known as '*straddling*' or '*satta karna*', and the speculator who does it is called a '*straddler*', '*straddle operator*' or '*spreader*'.

If the spread of Rs. 1.2.0 between the prices in Bombay and Hapur actually narrows down to (say) 12 annas, the straddle operator will make a profit of 6 annas a maund by settling his business in both markets, i.e. by buying in Bombay and by selling in Hapur. The settlement of straddle transactions is called '*reversal of straddle*' or '*satta torna*'. If, on the other hand, the difference between Bombay and Hapur widens to (say) Rs. 1.4.0, the straddler will suffer a loss of 2 annas per maund.

Hedging. Hedging is a kind of insurance—plying for safety. It is an operation whereby a business man by buying or selling futures protects himself against a price movement unfavourable to his ordinary trading transactions.

For example, a cotton mill company which has contracted to supply cloth at a certain price can either cover its future requirements by buying cotton futures or risk the turn of the market. In the latter case it will lose if the price of cotton rises, but it can guard against this contingency by speculating for a rise, that is, by buying cotton futures at the time it sells cloth for forward delivery.

A stockist of wheat might lose, if the price of his commodity fell. If, however, he sells wheat futures against his wheat stocks, he will make a profit in that way. At the first indication of a falling price, some stockists would, therefore, sell futures, that is, they would speculate for a fall.

Hedging differs from other forms of speculation in that its object is not to make profit, but to insure against loss.

Switching over. The process of transferring from one position to another (e.g., from Jeth contract to Bhadon) is known as *switching over* or '*satta karna*'. Thus, if a person who has bought or sold Jeth wheat finds that the prices are against him before the date of Jeth settlement but that they are likely to move in his favour thereafter, he may settle his Jeth business and enter into Bhadon contract, that is to say, he may switch over from Jeth to Bhadon.

Cornering. Where a number of bulls make a persistent effort to secure almost the whole supply of a particular commodity at a particular place, it is known as cornering the commodity.

Purchases. The demand for ready and forward goods comes from both genuine traders and speculators. Bull buying, bull support, bear covering, short covering, speculative buying, straddle buying, profit-taking or profit-

realising purchases, and stop-loss orders—all these are purchases made by speculators. Trade support, trade inquiry, trade buying, trade calling, trade price fixing, mill-fixing export inquiry are terms employed to indicate trade demand.

Sales. Sales are also made by both trade and speculators. A hedge sale is one made by a trader. A speculative sale may be made by either a bull or a bear, and speculative sales may be of several kinds. A bear sale, a blank sale or a short sale is one made by a bear. A straddle sale may be made by either a bull or a bear. Profit-taking or profit-realising sales are made by bulls. Bull liquidation or long liquidation means sales made by bulls whether at a profit or at a loss. Stop-loss sales, distress sales, tired liquidation, unloading by bulls—these are all sales, made by bulls at a loss.

Settlement. When a bull sells what he bought or when a bear buys what he sold, he is said to settle, square or switch off his deal.

Volume of Trading. The volume of business or trading done in a market on a particular day is expressed as brisk, moderate, restricted, limited, meagre, small, slow, stagnant, active, on a small scale, on a large scale, on a broad scale, little doing, nothing doing, not much doing, and so on. The market is said to be active, quiet, dull, uninteresting, featureless, colourless, eventful, uneventful, listless, stagnant, or neglected.

Prices The prices, rate or value of, or the basis, for a commodity does not remain the same, it fluctuates. Price fluctuations may be narrow, within narrow limits, within a narrow range, wide or violent. Very often two prices are quoted for a commodity at the same time—one buyer's and the other seller's, e. g., Rs. 3-2-5 $\frac{3}{4}$ buyer's and Rs. 3-2-6 seller's. The buyer's price is called value because it is the true price, '*Peak price*' or '*Ceiling of the market*', are terms indicating the highest price touched, whereas '*rockbottom price*' is the lowest price. The phrase "*With sellers over*" when attached to a price quotation means that the market is falling and that at that particular price, there are more sellers than buyers, e. g., "Rs. 3-2-6 sellers over" means that at this price there are no buyers, or, in other words, this price is nominal. Similarly the term "*With buyers over*" is employed when there are more buyers than sellers in a rising market.

When the opening and closing rates of a commodity for a day or for a week are compared, the result is expressed by phrases like the following: On balance there is a gain of 5 annas; over the week the rate has moved up by 5 annas; the net gain in the value is 5 annas, and so on.

Reaction. The term 'reaction' when used in connection with prices means a movement in the opposite direction. If the price of a commodity rises, it cannot go on rising; it must stop somewhere; and once the highest point is reached it must react or fall. When it begins to fall there is said to be a reaction. Similarly a reaction must come in a falling market.

Factors affecting prices. Anything which is likely to affect the present

and the future supply of and demand for a commodity will be responsible for its price fluctuations, and the principal factors affecting supply and demand are : (a) The statistical position and prospects of the commodity in the country and outside, that is to say, the existing stocks and the likely production ; (b) Vagaries of the weather ; (c) Government action (a. g., imposition or removal of import, export and excise duties, price control, restrictions on imports and exports, trade legislation, etc.) ; (d) Political situation particularly during the war ; (e) Sympathy with other commodities ; (f) Volume of imports and exports ; (g) Effect of substitutes ; (h) Sentiment created by rumours and sometimes even by jyotish in India ; (i) Foreign exchange fluctuations particularly the cross-rates, etc

Price fluctuations. The changes in commodity prices are usually expressed by the following words and phrases :—

Nouns and Adjectives : Rise, fall, decline, jump, setback, recession, rally, recovery, advance, gain, loss, up by, down by, upturn, upswing, bulge, landslide, apart, dip, flare up, break in values, depression, slump, relapse, drop, upsurge, improvement, sticky, jumpy, reaction, etc.

Verbs : Rise, fall, decline, jump, recede, rally, recover, advance, gain, lose, mark up, mark down, soar, barden, shoot up, shed, ease, steady, firm up, weaken, depress, slump, react, relapse, drop, tumble down, look up, drift down, move, improve, etc.

Rise or fall in prices may be marked, sudden, unexpected, sharp, smart, precipitous or abrupt. Phrases like slight improvement, partial recovery, mild rally, etc., are also commonly employed to express price fluctuations

Price ceiling and price floors are the highest and lowest prices fixed for certain commodities by Government.

Market Tone. The term 'tone' means the present tendency of prices. The words trend, mood, temper, sentiment, atmosphere and behaviour are also used in the same sense. The term 'undertone' or undercurrent' implies the future tendency of prices.

The tone of the market may be quiet, dull, uninteresting, easy, weak, bearish, steady at the decline, barely steady, steady, fully steady, firm, strong, bullish, healthy, confident, cheerful, buoyant, erratic, hesitant, irregular, indifferent, nervous, depressed, reactionary, optimistic or pessimistic.

Market Reports. The commodity and other market reports are a regular feature of the principal English, Hindi, and Urdu newspapers of the country. The English newspapers give more detailed and reliable commercial news, because they collect it either through their own special correspondents in the principal trade centres of India or through reliable news agencies such as A. P. I. (The Associated Press of India) or Reuters.

The market reports published in the newspapers are daily, weekly and annual. A daily market report has necessarily to be brief. It usually gives

the opening, highest and lowest rates of the day together with the closing rate of the previous day. It also indicates the tone of the market and a very brief reason for it. It is generally sent out in the afternoon. A weekly report reviews in detail the market conditions during the week and states the opening, closing, highest and lowest rates for the week together with a description of the factors responsible for the fluctuations during the week, and, in some cases also a very brief idea of the tendency during the coming week. Weekly reports are usually written on Saturday afternoons and appear in the Monday issues of the principal newspapers. An annual market report reviews a particular market for the whole year, is generally long and has to be drafted with special care.

The English daily newspapers that regularly publish daily and weekly market reports are the *Statesman*, the *Times of India* and the *Hindustan Times*; while the English commercial weeklies such as the *Commerce*, the *Capital* and the *Indian Finance* furnish more detailed weekly market reviews. An extremely useful publication entitled "*The Annual Market Review*", issued at the beginning of each year by Messrs. Premchand Roychand & Sons, Ltd., Bombay, contains excellent annual reviews of the principal markets of India. The annual market reviews also appear in the special annual numbers of the *Commerce*, the *Capital* and the *Indian Finance* issued at the beginning of each year. Amongst the Hindi and Urdu newspapers that publish market reports are the Urdu Daily *Tej* of Delhi, the Hindi *Hindustan* of Delhi, the Hindi *Daily Vyapar* of Hapur.

Test Questions

1. What do you understand by speculation? Discuss its relation with business. (Bombay B. Com. 1944)
2. Describe briefly the organisation and working of the E.I.C.A. or any other produce exchange in India. (Agra B. Com 1945)
3. Explain the organisation and working of any mandi or market you are familiar with. (Agra B. Com. 1947)
4. Write an essay on "Produce Market."

and industries would find it difficult to raise capital, for the investors would be afraid to invest their capital in industrial securities which cannot be converted into cash whenever necessary.

2. It enables investors to know the prices of their securities from day to day. This is achieved by means of its quotation service. The stock exchange quotations of the prices of scrips represent the average combined judgment of a large number of people, amongst whom are skilled financiers and expert business men. Because of the stock exchange, the opinion of these experts is made available even to the ordinary investor.

3. It directs the flow of capital from unprofitable to profitable industries. The stock exchange quotations of the value of securities enable the investors to know which industries are profitable and which are not. In the absence of this service, the capital resources of a country are likely to be used less efficiently.

4. It performs a very useful service through its listing regulations. When it admits to its 'list' any security, it does not, of course guarantee the value of the earning power of that security; but the fact that the exchange has admitted the security to its list carries a presumption in favour of its soundness. This is because of the fact that the company applying for the listing of its securities has to answer questions and supply information regarding its organisation etc.

Stock exchanges all over the world are not very old institutions. They have come with the development of joint stock enterprise on the principle of limited liability. The London Stock Exchange was founded in the year 1773. The Native Share and Stock Brokers' Association, Bombay (or the Bombay Stock Exchange, as it is popularly known) is the oldest stock exchange in India, having been founded in 1887. Long before the advent of this organised security market, dealings in securities were carried on in Bombay, but such dealings were not regulated by any code of rules. The Calcutta Stock Exchange was established in 1908 under the name of Calcutta Stock Exchange Association, which was registered in 1923 as a corporate body with a legal entity of its own. The Madras Stock Exchange, which ranks third in importance after Bombay and Calcutta, came into existence only in 1937. In recent years stock exchanges have also been started at Lahore, Cawnpore, Karachi, Ahmedabad, Delhi, Hyderabad and a few other places; but these are all in their infancy.

Constitution of Indian Stock Exchanges

Although there are a number of stock exchanges in India now, yet the Bombay Stock Exchange, being the oldest, occupies a position of supreme importance. It is truly a national institution where securities are dealt in by the people all over the country. The Calcutta and Madras Stock Exchanges are also rendering indispensable service to the investing public, as they specialise in certain securities which do not find a market in Bombay. The localisation of industries in different parts of India has tended to segregate the

several important groups of industrial securities in particular stock exchanges. For example, Bombay has become the chief market for textile shares, Calcutta concentrates more on jute, tea, coal and mining; Madras mainly confines itself to plantation industries. Ahmedabad has dealings mainly in local textile shares; Cawnpore deals principally in sugar shares; whereas steel shares are dealt in on all exchanges, but the bulk of the business is done at Bombay.

All the Indian stock exchanges are constituted more or less on the same lines, and all of them except the Bombay Stock Exchange are corporate bodies registered under the Indian Companies Act of 1913, with the liability of members limited by shares or by guarantee. The Bombay Native Share and Stock Brokers' Association is an unincorporated voluntary and non-profit body governed by a Deed of Association of 37 articles and by the rules approved and sanctioned by the Government of Bombay. Other stock exchanges in India are governed by their articles of association.

Each stock exchange consists of a number of members. On admission each member is charged an entrance fee which is a substantial amount these days. Membership cards fetch very high prices. All Indian stock exchanges other than Bombay, are companies having share capital divided into a number of shares, the holding of at least one of which is a condition of membership. An applicant for membership must be recommended by two members of the stock exchange and a candidate when elected is required to purchase one share and pay an entrance fee. The membership of the various stock exchanges is open to adults only, but the minimum age prescribed for a member by the Bombay Stock Exchange is 21.

The business on a stock exchange can be done only by its members or their authorised clerks. This is the privilege of membership. Members are bound by the rules and regulations of their respective exchanges. For breach of rules they have to pay penalties in the shape of fine, suspension or expulsion. Expulsion is, of course, a rare occurrence and happens only in case of fraud or criminal offence, or if a member is adjudicated an insolvent or becomes a lunatic.

On the Bombay Stock Exchange, besides its members, there are also persons known as 'Remisiers', who are 'half commission' men. They act as agents for the member brokers to secure business for them and are remunerated out of the commission received from the business secured by them. They are practically subject to the same restrictions as the members themselves. They are also prohibited from carrying on any other business and are required to deposit a substantial amount as security. In addition a remisier is required to pay an annual fee. Like a member broker he is not allowed to advertise. A remisier cannot make a bargain in his own name or on behalf of his employer unless he is also employed as an authorised clerk. A remisier is therefore a kind of sub-broker.

The members of a stock exchange are permitted to employ a number of

authorised clerks or assistants, but a prescribed annual fee is payable for each clerk or assistant. Authorised clerks and assistants can transact business on a stock exchange, but they can do so only on behalf of their employers. They cannot make any bargain in their own names. They simply act as agents of the members and transact business on the floor of the exchange on the basis of instructions given to them by their employers.

The administration of a stock exchange is vested in a committee of management, which is termed differently at different exchanges. At the Bombay Stock Exchange it is called a Governing Body, while at Madras a Council of Management. The strength of the committee depends upon the individual circumstances of each exchange. The election of the committee is made each year out of the members of the general body. The committee is the executive authority of a stock exchange, being vested with the general powers of supervision and management. The day-to-day management of a stock exchange is carried on by a number of sub-committees appointed by the committee of management.

Stock exchanges aim at safeguarding the interests of investors by regulating brokerage business and by maintaining a high standard of commercial morality among the brokers. For this purpose due precautions are taken in the admission of members. All possible care is exercised so that only persons of highest reputation and financial standing may be admitted to membership. Besides, all defaults on the part of members are carefully examined and duly punished. The constitution of a stock exchange provides rules relating to a variety of subject such as scales of brokerage, kinds of bids and offers permitted, maturity of contracts and their completion, clearing of securities, settlement and payment of transactions, transfer and registration of shares, etc.

Just as a bankers' clearing house is necessary for the banking business of a particular place, similarly a stock exchange clearing house is essential for the settlement of members' transactions. In India the system of clearing securities through the agency of a clearing house is of recent origin and was adopted in 1921 by the Bombay Stock Exchange. Stock exchange clearance involves both the clearing of securities and their payment; and a clearing house in fact acts as the settling department of the stock exchange. Clearing is made possible through the set-off of purchases and sales wherever possible and through the substitution of parties where set-off is not possible. Delivery and payment are centralised by bringing together the actual buyers and sellers and eliminating a number of intermediaries. It thus simplifies settlement by use of the simple device of setting off contra transactions, leaving only the net balance to be settled by actual payment.

The clearing house of the Bombay Stock Exchange is managed by the Bank of India, Ltd. Certain approved banks are members of the clearing house, and these banks in the first instance submit statements regarding the business of their constituents and then give or receive delivery. But such deliveries

and payments through banks do not form a large part of the total clearing at any time. Delivery and payment are also effected directly by the members themselves, though a smooth working of the clearing house is made possible through the co-operation of approved banks. Every member of the Stock Exchange has to maintain a current account at the Bank of India to facilitate clearing. The clearing house does not guarantee the title, genuineness or regularity of any security or transfer passing through it. It simply facilitates the clearing and payment of securities. Approved banks and investment trust companies are also allowed to act for members and their constituents for giving and taking of delivery and for receipting and making payment to the clearing house. Every member is allowed to have two clerks who are authorised to look after the clearing house routine and sign all papers. Every member is allotted a clearing house number which must appear on all forms used by the member in connection with clearing house operations.

Listing and Official Quotations

Listing The commodities bought and sold on a stock exchange consist of government securities, debentures and bonds of public bodies such as municipal corporations, port trusts, etc. and shares and debentures of limited companies. No dealings in the shares and debentures of a company can, however, take place on a stock exchange unless the necessary permission of the stock exchange committee has been obtained beforehand by the promoters of the concern. The shares and debentures of all companies existing in India are not dealt in on the stock exchanges, because many of them have not obtained the necessary permission from the stock exchange authorities. The brokers to a new company have an important function to perform in applying on behalf of the company for permission to deal in its shares on the stock exchange. The prospectus of a company usually contains a statement that application will be made to such and such stock exchanges for permission to deal in its shares and debentures, and those responsible for the issue of the prospectus must see that it complies with stock exchange requirements. Before a stock exchange allows its members to deal in any new shares or debentures of a company, its committee must give permission to deal. To obtain this permission the sponsors for the security must supply, through a member of the stock exchange, the required information.

Listing constitutes an integral part of the machinery of an organised stock exchange. Dealings in corporate securities, by their very nature, are susceptible to fraud and undesirable practices, hence the necessity for listing arises. Listing implies that the securities, when they have been admitted to dealings on a stock exchange, would meet, to the satisfaction of stock exchange authorities, certain prescribed standard of legality, security and workmanship. When a security is admitted to dealings, the soundness of the issuing company is in no way guaranteed, nor is the security recommended for any favourable consideration. The investor himself has to exercise his own discretion in selecting a

particular scrip. The stock-exchange cannot be expected to act as a judge and advise the investors regarding the soundness or otherwise of a particular company. This would be imposing a responsibility on the stock exchange committee which it would be incapable of carrying out. The company law of a country and the listing requirements of a stock exchange call for certain information which is to be published and will act as a basis for the discretion of investors. The work of the stock exchange committee is to see that the provisions of the company law have been complied with and the investors are given a reasonable opportunity of judging the merits of the concern.

A stock exchange, before granting permission to deal, requires the observance of a set of rules by the company and calls for certain information with a view to protecting the investors. The information supplied by the company is examined impartially and permission is granted or refused. This permission naturally carries a presumption in favour of the company's soundness and indicates that at the time of listing it is legally organised and is solvent as a going concern. The listing does not provide any guarantee regarding the earning power of listed securities; but the privilege of listing does create a favourable impression on the minds of investors who are indirectly assured of the soundness and legality of the company.

At the same time, listing provides shares and debentures the benefit of a continuous market where sales can be effected without any waste of time. It thus adds to the collateral value of the security which can be so easily hypothecated for a loan. Business in listed securities is transacted under certain regulated principles, and both the buyers and sellers are thus afforded a certain degree of protection. Investors and dealers can also obtain the benefit of a regular and systematic quotation service and are assured of the price of securities which can be converted into cash at approximately the prevailing rates.

In companies listing affords a distinct advantage because listed securities occupy a certain degree of prestige in the minds of the public. Their securities are popularised and made public through the agency of the quotation service of a stock exchange and find a place in the daily quotation list of newspapers.

The listing requirements of London and New York, Stock Exchanges are very rigid, but that is not the case with Indian stock exchanges, because our company law itself requires the publication of a good deal of vital information relating to the affairs of companies. A company, seeking the privilege of admission of its securities to dealings on a stock exchange, must have been registered under the Indian Companies Act, and its prospectus must be published in some newspapers. It should undertake to comply with certain prescribed conditions, e. g., it should agree not to close its transfer books on such days as may be inconvenient to the stock exchange, its articles of association must contain some particular provisions, it must supply certain information to the

stock exchange, and so on. A stock exchange retains the power to remove any shares from its list, if the company has failed to comply with the proscribed conditions.

Quotation list. An official quotation list is published daily by all important stock exchanges. The official lists contain the various prices at which business has been transacted and also a description of lots in which business took place at particular prices. An official quotation list is divided into several sections. Quotations are taken from the boards displayed in the various markets of a stock exchange.

STOCK EXCHANGE TERMS

Securities. It is a common term used for the commodities dealt in on a stock exchange and includes government securities, debentures and bonds of public bodies, and shares and debentures of companies. Promissory notes or bonds issued by the Central Government or Provincial Governments for monies borrowed from the public are called *government securities* or *gilt-edge securities* (or merely *gilts*), as they are first-class securities which give the investor the greatest possible degree of safety.

The securities, which from the point of view of safety approach government securities, e.g., shares and bonds which carry a government guarantee as to principal and interest, may be referred to as *semi-gilt edge*. Those securities, which from an investor's point of view may be considered sound both as regards the income to be derived from them and as regards the repayment of capital invested in them, are known as *investment securities*, which usually include debentures and shares of banks, insurance and public utilities concerns. *Trustee securities* are those in which trust funds can be legally invested, e.g., government securities and debentures of local authorities.

Nominal Value The face value of a security is called its nominal value, but its actual market price is seldom the same as its nominal value. The market price of a security is governed by many factors such as the income obtainable from the security, the prevailing rate of interest, the political situation existing at any particular time, safety of capital, the possibility of capital appreciation or depreciation, the volume of speculation in the market, and so on.

Market Price. This is the price of a security at which holders are willing to sell and the purchasers prepared to buy it. The factors affecting the prices of securities have been briefly referred to above. When the price of a security is the same as the nominal value, it is said to be *at par*; when it is lower than the nominal value it is said to be *at a discount*; and when it exceeds the nominal value, it is said to be *at a premium*.

Ready and Forward Business Dealings on a stock exchange are of two kinds: Ready and Forward. In the first case, the transaction is completed at once or in a few days; while in the other the delivery and payment are both postponed to a future date. On all organised stock exchanges the forward

business done is settled on certain fixed dates known as *settlement days*. The forward business which goes under the name of *raida* business is usually settled every month, and the settlement of forward business is effected through the agency of a clearing house.

Scrip This is a common term employed on the stock exchange for any kind of security, such as government paper, debentures and shares. The term 'stock' is also used in the same sense. Shares of companies are often called *counters*, *issues* or *units*. Shares of industrial companies as distinct from banks or insurance and public utility companies are known as *industrials*.

Equity Shares (or merely '*Equities*') are the ordinary shares of companies. Those shares in which speculative business is usually carried on are called *speculative counters*.

Budla or Carry-over. A speculator who has bought or sold a security for forward delivery may be unable to pay for it or to deliver it on the settlement day, and therefore he may desire the completion of the transaction to be postponed to the next settlement. This is called '*carry-over*' or '*Budla*'. A rate paid by a bull to enable him to renew a bargain until a later settlement is known as *contango*, while a rate paid by a bear to enable him to renew a bargain until a later settlement is called *backwardation*.

s. l. or s. o. l. (small lots or small odd lots) are abbreviations often attached to price quotations and indicate that only a small business was transacted, and therefore the quotations given may not be taken as a fair indication of the price movement.

Buying-in and Selling-out. Buying in is the process by which a buyer enforces delivery of securities when the seller has failed to deliver them within the stated time. Selling-out is effected by the seller when the buyer refused to take delivery of shares and fails to pay for them.

Bearer and Registered Securities. Securities, the possession of which is in itself evidence of ownership, are called bearer securities, and they can be transferred by mere delivery. Securities, the holders of which are registered in the books of the authority issuing them, are called registered securities, and they can be transferred only by means of a written instrument.

Cum-Dividend and Ex-Dividend. These terms are frequently attached to the price quotations of stock exchange securities. The term cum-dividend (cum-div. or simply c. d.) means that the price quoted includes the interest accrued or the dividend announced on the security. In the case of government securities or debentures, carrying a fixed rate of interest, usually payable twice a year, the cum-dividend quotation includes the net interest (i. e., gross interest less income-tax) accrued thereon from the date of last interest payment up to the date of quotation; and in such cases, the price quotation is always a cum-dividend quotation whether the abbreviation c. d. is used or not unless started otherwise. In the case of company shares, however, a quotation will be cum-dividend only after a dividend thereon has been announced by the

1. A company paid for 1945 a dividend of Rs. 10 per share free of tax on its Rs. 100 fully-paid shares quoted at Rs. 165 ex-dividend. The yield on these shares works out to 6.06% free of tax. That is to say, an investor who purchases one share will have to pay Rs. 165 on which he may expect a dividend of Rs. 10 if the last year's rate of dividend is maintained. But if the future prospects of the company suggest that the dividend for the current year may be raised to Rs. 12 per share free of tax, then the yield will be 7.3% tax-free.

2. A company paid for 1945 a dividend of 20% free of tax on its Rs. 10 fully-paid shares quoted at Rs. 60 cum-dividend. Deducting the accrued dividend of Rs. 2 from the cum-dividend quotation, the ex-dividend price comes to Rs. 58 per share, and yield thereon is 3.45% free of tax.

3. A company paid for 1945 an interim dividend of 8% and a final dividend of 26% on its Rs. 50 fully-paid shares quoted at Rs. 312½ cum-dividend. Here the dividend included in the quotation is only the final dividend, namely, Rs. 14 per share. The ex-dividend price works out to Rs. 298.80 and the expected annual dividend on the basis of the last year's dividend is Rs. 18 per share. Therefore the yield comes to nearly 6%.

4. A company paid for 1945 an interim dividend of 22½% and a final dividend of 22½% on its Rs. 25 fully-paid shares quoted at Rs. 214 ex-dividend. The yield on these shares is 5.26%.

Sometimes the market quotation of the shares of a company includes not only the dividend declared thereon but also the value of rights attached to them. Such a market quotation is known as the cum-dividend cum-rights price. The rights referred to in the market quotation may be either a right to the new issue of shares at concessional rates or a right to the free issue of bonus shares. In calculating the yield on a share which is quoted cum-dividend cum-rights, the value of the dividend and the value of the rights included in the quotation must be ascertained and the ex-dividend ex-rights price of the share worked out. How this should be done is described in the following illustration.

A company has an issued and fully-paid share capital of Rs. 10,00,000 in Rs. 100 shares. It increases its share capital by the creation of 5,000 new shares of Rs. 100 each, which are to be offered to the existing shareholders at Rs. 205 each in the proportion of one new share for every two old shares held. The company has also declared a dividend of Rs. 15 per share for the last year. The market quotation of the shares after the declaration of dividend and the announcement of rights is Rs. 265 per share cum-dividend cum-rights. The yield in this case will be computed as follows:—

			Rs.
Cum-dividend cum-rights price	...	...	265
Less the amount of dividend included therein	...	...	15
Therefore the ex-dividend cum-rights price is	...	...	<u>250</u>

The ex.dividend cum-rights price of two shares which must be bought in order to be entitled to a new share at concessional rate will be	... 500
Add the amount to be paid to the company for a new share	... 205

Therefore the ex-dividend ex-rights price of three shares becomes

Or, the x. d. x. r price of a share is ... 235

In other words, the value of rights attached to each share is Rs. 15.

Now a dividend of Rs. 15 is expected on a capital of Rs. 235. Therefore the yield comes to 6.4%

If in the above illustration the company does not issue fresh capital at concessional rates, but it issues one free bonus share for every four shares held, then the yield will be worked out as under :—

The ex-dividend cum-rights price of four shares which must be purchased in order to secure a free bonus share is Rs. 1,000. That is to say, by investing Rs. 1,000 a shareholder becomes entitled to a free bonus share. In other words, the ex-dividend ex-rights price of five shares is Rs. 1,000 or the ex-dividend ex-rights price of a share is Rs. 200 on which a dividend of Rs. 15 may be expected. Therefore the yield works out to 7.5%.

Take another illustration. A company's issued capital consists of Rs. 10 fully-paid ordinary shares. It prepares half-yearly accounts and it has just declared a dividend of Rs. 4 per share free of tax for the last half-year. It also declares a capital bonus by issuing one free Rs. 10 fully-paid preference share as a bonus share for every five ordinary shares held. After the declaration of the dividend and the capital bonus, the market price of its ordinary shares is quoted at Rs. 92½ cum-dividend cum-rights; and it is also expected that the preference shares issued as bonus shares will have a market quotation of Rs. 15 each. In such circumstances the yield will be calculated as follows :—

	Rs.	a.	p.
The cum-dividend cum-rights price of an ordinary share	92	8	0
Less the amount of dividend included therein	...	4	0
Therefore the x. d. c. r. price of an ordinary share is	...	88	8

Now for every five ordinary shares held one free preference share is received as a bonus share, and the expected market price of this bonus share is to be Rs. 15. Therefore Rs. 3 is the value of the bonus right attached to each ordinary share, and the ex-dividend ex-rights price of an ordinary share will be (Rs. 88-8-0 minus Rs. 3) or Rs. 85-8-0, on which a half-yearly dividend of Rs. 4 or an annual dividend of Rs. 8 is expected. The yield will then come to 9.4%.

Break-up Value of Shares. Sometimes it may be necessary to calculate the break-up value of the shares of a company, particularly when their market

price is standing at a figure not warranted by the financial position of the company. The break-up value of a share means the amount obtained by dividing the net assets (i.e., total assets minus liabilities) by the number of shares issued. The break-up value of the shares of a company may, therefore, be calculated as follows :—

1. Find out the amount of net assets by deducting from total assets the amount of liabilities after allowing for a probable loss or a possible profit on the balance sheet values.

2. If there are shares of one class only, divide the amount of net assets by the number of shares issued, and the resulting figure will be the amount of the break-up value of each share.

3. If there are both ordinary and preference shares, ascertain the rights attached to preference shares in respect of dividend and repayment of capital. Where the preference shares have priority as to repayment of capital on a winding-up, they will be valued at par, and the balance of the net assets will be divided by the number of ordinary shares issued, which will give the break-up value of each ordinary share. Where, however, the preference shares have no priority as to the return of capital on a winding-up, they rank *pari passu* with the ordinary shares; and the net assets of the company are deemed to be the combined property of the holders of both classes of shares, and will be apportioned between them according to the amount of their paid-up capital. The preference share-holders' portion of the net assets will then be divided by the number of preference shares issued and the ordinary shareholders' portion by the number of ordinary shares issued, thus giving the break-up value of each preference as well as ordinary share.

This principle may be illustrated by means of an example. Suppose the following is the balance sheet of a company as on 31st December 1945 :—

	Rs.	Total Assets	Rs.
2 000 6% Preference Shares of			14,00,000
Rs. 100 each fully-paid	2,00,000		
40,000 Ordinary Shares of			
Rs. 10 each fully-paid	4,00,000		
Reserves	4,00,000		
Liabilities	3,00,000		
Profit & Loss Account	1,00,000		
	<u>14,00,000</u>		<u>14,00,000</u>

The net assets of this company amount to Rs. 11,00,000. If the preference shares have a priority as to repayment of capital in the event of the company's winding up, then each preference share is worth Rs. 100, leaving Rs. 9,00,000 for the net assets for the ordinary shares. Each ordinary share will then have a break-up value of Rs. 22½. If, however, the preference shares rank *pari passu* with the ordinary shares, the net assets of the company amounting to

Rs. 11,00,000 will be apportioned between the preference and ordinary shareholders in the ratio of their respective capitals, namely, in the ratio of 1 and 2. The preference shareholders' portion of the net assets will be Rs. 3,66,666.10.8 and the ordinary shareholders' portion Rs. 7,33,333.5.4. Rs. 3,66,666.10.8 divided by 2,000 will give the break-up value of each preference share, and Rs. 7,33,333.5.4 divided by 40,000 will give the break-up value of each ordinary share.

In making these calculations, any contingent assets not appearing on the balance sheet should also be taken into account. At the present time such contingent assets consist of the post-war refunds of E.P.T. paid and the interest payable by Government on the E.P.T. compulsory deposits.

Tout. This term is used for a canvasser who brings business to a member of a stock exchange. Strictly speaking toutting is contrary to the rules of an organised stock exchange, but in practice it is common.

Tip. The information of an event about to take place, which is likely to affect the price of stock exchange securities, is known as a tip. The person who gives away tips is known as a tipster.

Short-Selling and Cornering. Short-selling is the process of selling a security which one does not possess in the hope of a fall in prices, when the sale will be covered by making a purchase. The terms bear and short are the same. Short selling is inherently speculative and excessive short-selling may sometimes lead to cornering. A corner arises when more shares than are available for delivery on the day of settlement have been sold and the buyer holds the sellers to ransom. What really happens when a corner exists is that an individual or a group succeed in obtaining possession of all the shares of a certain company, and at the same time they enter into contracts with short-sellers to buy the same shares, when the time comes for delivery the short-sellers are unable to deliver the shares (as the shares are held by the individual or the group) with the result that they have to buy the shares from the very persons at a price dictated by them.

Strictly speaking, it is the controlling of shares with the sole object of inflating their prices that can be called a corner, but the usual procedure followed in a corner is the accumulation of floating supply of stock and the stimulation of a large short interest. When such a situation develops anyone short of the security is at the mercy of the cornering persons who can charge as exorbitant a price as they like.

Options Option dealings or teji-mandi transactions form an intricate and technical method of speculation. They have already been explained in the previous chapter, along with certain other terms.

Transaction of Business

Business on a stock exchange can be conducted only through a broker who is a member of the stock exchange, therefore a person wishing to do business on a stock market is required to come in contact with a broker. Before opening

an account with a new client, stock brokers usually require a personal introduction or a bank reference, so that they may know the standing and credit of their would-be clients. The business transacted on a stock exchange is of two kinds - Ready delivery business and Forward delivery business.

Ready Delivery Business. A ready delivery contract is a contract for the purchase or sale of securities, for the performance of which no time is specified and which is to be performed immediately or within a reasonable time, which is a question of fact in each particular case. For example, Regulation 331 of the Bombay Stock Exchange provides that :—

"A bargain for ready delivery shall be for delivery and payment before 3 p.m. on the business day next following the bargain. If such day is Saturday, delivery and payment shall be made on the business day next following, provided that if the parties expressly stipulate at the time of the bargain, a bargain for ready delivery shall not be deemed invalid if delivery of and payment for the stock is made not later than seven days from the date of the contract." Thus a period of seven days is allowed for delivery and payment in case of bargains for money. At the Calcutta Stock Exchange the buyer has to make arrangement for cash on the third day after the bargain and the practice of Madras Stock Exchange is the same as that of Bombay and seven days are allowed for delivery and payment.

The brokers through whom ready delivery contracts are made attend to the formalities necessary for the giving and taking delivery of shares, such as the completion of the transfer deed and its registration in the books of the company.

Forward Delivery Business. Forward delivery contracts or *dealings for the account*, as they are commonly called, imply that the transactions will be taken up, paid for or differenced on the next settlement. Such transactions are sometimes called time bargains because some period must elapse from the time they are made to the day they are closed, and during this period the price of the security may materially alter in favour of or against the speculator. A forward delivery contract may, however, be closed at any time before the settlement and the speculator is thus able to take advantage of any variations in the price of the security. A very large majority of the forward delivery bargains are purely of a speculative character. They are effected by persons who do not want to pay for and take delivery of securities they have contracted to purchase, or who do not possess the stock they have contracted to sell. Such dealers anticipate that they will be able to sell or buy at a profit before the settlement day and make a profit in 'differences' of prices.

Settlement of Forward Delivery Contracts. Forward dealings are settled periodically, e.g., once a month. Forward delivery bargains are made not with the intention of taking or giving delivery and making payment but with the intention of making a profit from the buying and selling operations during the course of the settlement period. Legally every contract for sale

connotes an intent to deliver the shares, but in practice it seldom happens. The settlement of forward delivery bargains is made by the clearing house. On the settlement day either delivery is taken or the transaction is reversed, i. e., a purchase is reversed by sale and *vice versa*, the difference being claimed or received, or it is carried over.

Buying-in and Selling-out. If the seller in the case of ready delivery contracts fails to deliver the securities the securities are bought-in against him, and if a buyer refuses to take delivery of securities and pay for them, the securities are sold-out on his account. Similarly, in case of forward transactions if a member fails to pay within the time prescribed, the securities are sold-out; and if there is a default on the part of the seller, the buyer may buy-in the securities, but if it is not possible to buy-in the securities, the matter can be referred to arbitration.

Reversing of Transactions. As a general rule, forward bargains are entered into with the object of taking advantage of market fluctuations and to reverse them before the settlement, thereby receiving or paying the difference. Such differences are paid or received on the basis of the prices prevailing in the market at the time of settling.

Carry-over or Budla. The carry-over or budla means the postponement of the bargain to the next settlement. The budla is effected and the budla brokers' fee is paid in order to postpone payment or delivery from one settlement to another. This is in fact the continuance of purchases and sales without their closure. Carry-over is resorted to when the prices do not move according to the expectations of the parties concerned. Budla is effected by means of two new bargains. A bull transaction is carried over by a sale for current settlement and repurchase for the next. A bear transaction is made a budla by a purchase for the current settlement and resale for the next. The net result of the budla is that the original bargain is completed for the current settlement and a new transaction at new prices is opened up for the next settlement.

The bull operator who has contracted to buy but who does not himself pay for the securities purchased or who does not possess ready money to pay against the delivery of securities, may approach a budliwala for credit. There are a number of persons known as budliwalas who conduct the business of affording financial facilities for carry-over. They lend money to the bulls against the pledge of their securities and charge a comparatively high rate of interest.

Alternatively, it may be arranged that the seller will not press for payment against the delivery of shares and in return may charge an interest from the purchaser for accommodating him. This in fact implies that the bull operator has borrowed money from the seller and the settlement is postponed in consideration of an agreed amount of interest. This payment by the buyer to the seller is known as budla charge or contango.

Similarly if a bear has no securities to deliver on the settlement day, he may be required to borrow them with a view to delivering them to the purchaser. This may be avoided by arranging to pay a certain amount to the bull who would agree to defer delivery of securities. This payment is known as *budla* charge or *backwardation*.

An illustrative transaction. The science of investment may be summed up as the art of safe and remunerative employment of money. *Greed in the matter of interest may lead to grief in the matter of capital.* A person wishing to invest his money in stock exchange securities must ask himself the question whether he wants to eat or to sleep, i.e., whether he wants to go in for speculative securities or for sound ones. It is not difficult to say that a certain share is worth buying, but it is difficult to say when is the time to buy it. Advice should be sought from one with experience and knowledge and who is provided with these two rare qualities—common sense and judgment. The great difficulty is that the public—that is to say, investors generally—are very much like the proverbial flock of sheep. When things look black nobody can be persuaded to see daylight anywhere. On the other hand, when prices are booming they see no limit to the upward movement. The red light is disregarded; they become colour-blind from inclination.

Let us assume that Mr. Shambhu Nath of Agra, who has some Rs. 5,000 to invest in stock exchange securities, has decided on the advice of an expert in investment matters (e.g., a share broker or a bank) to purchase ten fully-paid Rs. 100 shares of the Western India Match Co., Ltd., which are quoted in the market at Rs. 420. These shares are dealt in on the Bombay Stock Exchange, and therefore he must take the necessary steps to buy them in that market. The procedure that he should adopt for this purpose will be as follows:—

1. He may write to his bank in Agra to purchase these shares for him, or he may authorise a local agent (if any) of some Bombay broker to purchase these shares for him, or he may directly deal with a Bombay broker who must be a member of the Bombay Stock Exchange. The first course is rather expensive, because, besides the brokerage, he will have to pay the bank commission. Banks do not operate on the stock exchange; they have to utilise the services of stock brokers who are members of a stock exchange. The second course is rather risky. The local agent may not be very reliable and Mr. Shambhu Nath may be duped. The last method, is, therefore, the best for him, but here he must take jolly good care to select a reliable broker.

Under the present rules of our stock exchanges, any moneyed man can purchase a card or a share of a stock exchange and become entitled to its membership, no period of training or apprenticeship being necessary. The stock exchange authorities do not insist on any minimum qualification of members. The stock exchange business is highly technical. To enter into such a business without any knowledge, experience or training is simply to court disaster. Though every stock exchange in this country can boast of a

good handful of competent, honest and knowledgeable brokers, yet most of the brokers are not such as may be safely employed by lay clients. Let us assume that Shambhu Nath has fortunately selected Messrs. Imandar & Co., a reliable firm of share brokers in Bombay who are members of the Bombay Stock Exchange.

2. He will place a written order with Imandar & Co. for the purchase of ten shares³ of Western India Match Co., Ltd, either at a named price (say, up to Rs. 420) or at the best obtainable price without placing any limit. If he forwards a bank draft for the approximate cost of shares, his order will be at once booked by the brokers. But if he wants to pay after the purchase is completed and if he has not done any previous business with Imandar & Co., the latter will require a bank reference before accepting his order. We may assume for our purpose that a bank draft of Rs. 4,500 is enclosed with the order.

3. On receipt of this order with a sufficient remittance, the brokers will proceed to make the purchase. First of all they will find out from their orders received book whether any client of theirs has ordered the sale of the same scrip without imposing any particular price. If there is one, they will effect the purchase and sale in their own office without recourse to the stock exchange and inform both the clients accordingly. Such a deal is known as a cross transaction (C. T.) If they have no such order to sell on their book, they will send one of their authorised clerks (Mr. Dalal) to the Stock Exchange hall where transactions take place. Nobody can visit the hall unless he is a member or an accredited agent of a member. In the trading hall groups of people are assembled here and there and they talk in a language which is intelligible only to those present there. An outsider will get simply confused and bewildered, and yet it is a place where people make or lose fortunes. Mr. Dalal goes to a corner, meets a dealer Mr. Somani who more or less specialises in Wimco shares, and after a little higgling strikes a bargain at Rs. 415. Pencils and note books come out and both parties enter the bargain. Mr. Dalal will enter on the bought side of his note book "Bought ten Wimco shares from Somani at Rs. 415 for Mr. Shambhu Nath of Agra", and Somani will record on the sold side of his note book "Sold ten Wimco shares at Rs. 415 to Imandar & Co."

After this Mr. Dalal will go in a central place where a black board is placed. This is known as the 'marking board.' The latest transactions are posted on this board for the information of dealers. A box is placed under the marking board. Dalal enters the bargain on a slip of paper under his signature and drops it in the box. The next moment this price is posted and the one at which a previous transaction had taken place in this scrip is rubbed off. The closing prices of all securities dealt in on a particular day are then recorded in the official quotation, and those of the principal scrips are broadcast over the radio and also appear in the next day's newspapers.

4. From the dealing books of the two brokers bargains are entered in their ledgers. Both the brokers will check the transaction next morning from

their note books and will prepare Contract Notes and Bought and Sold Notes for their clients. Imandar & Co. will make out a Contract Note and a Bought Note and will forward them to Shambhu Nath with a covering letter. The Contract Note will be signed by Shambhu Nath and returned to the broker, the Bought Note being retained by him to serve as evidence of the transaction.

5. The terms of delivery and payment are not uniform on all stock exchanges. The parties have to abide by those rules, and in case of default the aggrieved party can represent to the Stock Exchange Committee who will authorise to buy-in or sell-out as the case may be, at the cost of the other party. Mr. Somani will similarly send a Contract Note and a Sold Note to his client, who will return the Contract Note duly signed by him. On receipt of it the broker will send a blank form of transfer deed to the client requesting the latter to execute and return it along the share certificate. On receipt of these documents, Somani will deliver them to Imandar & Co. against full payment.

6. Finally, Imandar & Co. will arrange for the registration of the transfer in the books of the Western India Match Co., Ltd., and will in due course receive a share certificate in the name of Shambhu Nath. They will then send the share certificate to him along with a statement of account showing the full cost of the purchase and returning any excess money received from him.

Stock Exchange Speculation

Speculation is closely associated with the business of a stock exchange. Speculation performs a very useful function in the economic life of the community. It is very difficult to draw a line between legitimate business and speculation either on the stock exchanges or elsewhere. The word speculation is derived from the Latin '*Speculare*' meaning to look at from afar. Speculation therefore implies visualisation of future events and occurrences. Speculation on a market means buying and selling of commodities with a view to making profit from the differences between present and future prices.

It is wrong to say that a person who speculates in stocks and shares is in any way morally inferior to anyone who buys them for investment. In fact, a speculator performs an economic service to the community. By increasing the number of dealings in stocks and shares in which he operates, he creates a market, thus enabling investors to buy or sell on more favourable terms. The proper function of speculation is to bring about an equilibrium of demand and supply in the market and thus to facilitate the smooth course of consumption, production and exchange. This is achieved by speculation through steadying prices. It is the presence of speculators at the various exchanges that a continuous market is guaranteed. A continuous market may be defined as one where any security listed in the market may be bought or sold at any time during business hours at comparatively small variation from the current price.

Healthy speculation, which is based on scientific knowledge of business conditions and proper forecasts, benefits not only the speculator but the society as well. A speculator's object is to make profit by mitigating the rise or fall in prices. His profits are as it were a reward paid to him by the community for mitigating price changes. When speculation is based on correct estimates of future price changes, the result is necessarily a reduction in violent price fluctuations. Just as healthy speculation is beneficial to society, similarly unhealthy speculation leads to great injury and waste. When speculation is carried on by amateurs on the basis of unfounded rumours and imperfect knowledge of economic events, it instead of reducing price fluctuations tends to maximise them and leads to much economic waste. Again, when speculators selfishly try to alter prices by artificial means in order to fill their own pockets, they become a curse to the market and cause a great loss to the public. It is, therefore in the general interest of society to foster healthy and curb unhealthy speculation.

Speculation and Investment Though it is not possible to draw a clear line of distinction between speculation and investment on a stock exchange, yet it may be pointed out that a pure investor is one who looks for a fixed income with a certainty of return of capital and does not care much for capital appreciation in the value of his holdings. An investor who buys a security with the primary intention of holding it more or less permanently has to employ his own capital. A speculator, on the other hand, is little concerned with the periodic income of his securities and regards it as accidental only. He purchases a security with the primary intention of selling it at a profit and usually employs borrowed capital. The dealings of a speculator are mainly based on differences in prices. The difference between a speculator and an investor is a matter of motive. The real investor looks most of all to the security of income and least to the hope of capital appreciation, while the pure speculator has no particular regard for income but looks entirely to the chance of being able to make a big profit by resale.

Speculation and Gambling. It is difficult to differentiate between these two terms and to say where speculation ends and gambling begins. The distinction between speculation and gambling is more ethical than economic. The exercise of brains by the speculator distinguishes him from the gambler to a large extent. A speculator forms his ideas of the future from knowledge and experience, whereas the gambler simply guesses. Gambling is based on blind chance, but speculation has some basis for its operation. Speculation and gambling can also be distinguished by dividing speculators into two classes—professionals and amateurs, the latter speculating without any knowledge or skill in forecasting future changes in demand and supply and consequent changes in prices. They do so in a gambling spirit and often follow false prophets. On the other hand, professional speculators are shrewd business men, who have made speculation their business, and who on account of their

superior knowledge and foresight are able to forecast the future with considerable accuracy. The legal distinction between speculation and gambling is clearly made out in the following note which appeared in "*Capital*" of 3rd February 1938.

"The distinction between speculation and gambling is a fine one and it is often difficult to distinguish between the two. Yet, as the law looks with tolerance on speculation but with a jaundiced eye on its only slightly more erratic twin brother, it is of considerable importance to ascertain what principles there are whereby the difference between them can be made clear and a particular transaction definitely labelled as belonging to one category or the other. There is nothing illegal in speculating. It is a commonplace of the Stock Exchange. The law, on the other hand, strikes at gambling.

"A very large number of dealings on the Stock Exchange are of a speculative nature; persons buy and sell shares for a future date with the hope of making a profit by the rise or fall in price and often with the least intention, or even ability, either to pay for the securities or to deliver them, but meaning to resell or re-purchase before the time for delivery arrives. This method of doing business is by no means confined to stock and shares but is of everyday occurrence in almost all commodities; and as far as the distinction between speculation and gaming is concerned, it makes but little difference whether the commodities are actually paid for and held with a view to selling again at a profit, or whether the matter is arranged by a re-sale before the time for delivery. Such dealings are perfectly legitimate. Gaming and wagering contracts, on the other hand, are not real dealings at all; they may take the form of purchases and sales but they are in fact mere bets on the market price of commodities at a future date. For a contract to be a gaming and wagering contract, there must be not only no *intention* on the part of either party to deliver or take delivery of the commodities, but also no *obligation* on either to do so; there must be an agreement or understanding that all the buyer has to do is to receive from or pay to the seller the difference between the price of the bargain and the price at some future date. Further, the essence of gaming and wagering is that one party is to win and another to lose upon a further event, which, at the time of the contract, is of an uncertain nature.

"Thus the difference between the two is to be found in seeing whether the transaction in question is a real transaction or whether it is merely a peg to hang a bet upon; and whether it is a real transaction depends upon whether in law the parties could be compelled to carry out the contract of sale."

Kinds of Speculators. The stock exchange speculators are of three kinds—the bull, the bear and the stag. They do not possess all the characteristics of their namesakes of the jungle, but they have certain peculiarities of their own, nor is it necessary that a bull operator always acts as a bull and a bear as a bear. The same operator may be a bull and a bear at the same time.

A *bull* (or a '*long*') is an operator who purchases a security for forward

delivery in the hope of being able to sell it at a profit before the date of settlement. He does not intend to take delivery of it and pay for it. The idea of such operators is to sell the securities which they have purchased before the settlement day. If the expectations of the bull materialise and the rise in prices takes place, he sells out the securities without paying any money for their purchase, and he pockets the difference between the buying and selling rates less expenses. On the other hand, if the price falls against his expectations, he may pay the difference as a loss, or else he may carry forward a transaction by paying a *contango* or *hudda charge*.

A *bear* (or a *'short'*) is a speculator who contracts to sell for forward delivery stocks, shares and other securities which he does not possess. He always hopes for a fall in prices which would enable him to buy the scrips at a price lower than that contracted for and before the date of delivery, thus making a profit on the transaction. If, contrary to his expectations, the market price goes up and he is forced to buy back his security at a higher price than that at which he has sold, he pays the difference which is a loss to him. Like a bull he may also carry forward a transaction by paying a *backwardation* or *hudda charge*.

A *stag* is a speculator who neither buys nor sells but who merely applies. He is the operator who applies for shares in a new company with the object of selling them as soon as a premium is obtainable. He does not intend to put down more than his application money, since he hopes to sell before even allotment money is called. In this way he can apply for a much bigger allotment than his means permit. A stag may sometimes sell the shares before allotment, anticipating a successful allotment to himself. He may do this as a kind of preliminary manoeuvre, hoping that the promoters will buy from him rather than see the market in their shares spoilt by premature selling.

The operations of stags (known as *staggering*) are not free from risk. If the response to a public issue, in which a stag has applied for a large number of shares, happens to be small, he would find that his offer has been allotted in full and the price of such shares in the market may open at a discount. This may entail a heavy loss to him unless he decides to take up the allotment, pay for it and then wait for a considerable period. This course, however, will be available only if he commands ample financial resources.

What is stated above is the original meaning of stag. But the term stag is also being employed for a person who buys securities, even government securities, mostly with bank loans, the loans being taken by pledging such securities. He does so in the hope that there will be a rise in prices and he will be able to sell his holding at a profit thus repaying the bank loans. In that respect he resembles a bull, and he may, therefore, be termed a bull in the making.

Speculation on Indian Stock Exchanges

Stock exchanges are meant to provide facilities for healthy speculation, so that the investors may be assured of a constant market in their scrips.

Hence along with investment business a certain amount of speculation must always find its way and is also desirable. But unhealthy speculation is a menace and must be eradicated from a well-organised stock exchange. The Bombay Stock Exchange is notorious for wild speculation. Of the total business transacted there, much too high a proportion is of a speculative nature. The Calcutta and Madras Stock Exchanges too are not free from the speculative mania of the operators and are becoming highly speculative in outlook. The reasons for the wild speculation that has taken place in recent years are graphically described in the following extracts taken from "Indian Finance" of January 6 and 13, 1945:—

Whatever may be the ostensible reason for the rise in shares the real fact is that people have a large amount of idle money on their hands and there is no channel for its employment except the stock exchange.

(1) I was talking the other day to an old operator on the market. He said "Conditions on the Calcutta Stock Exchange have changed so much in the last, three or four years that it is almost impossible to judge the market. In the old days if a broker, who called on some people connected with managing agency firms, received some order he would walk leisurely inside the Exchange, talk to several parties interested in the particular security he was interested in, and then buy what he had to buy. Shrewd operators would keep a watch as to who was buying and who was selling and regulate their operations accordingly. But now-a-days if you talk inside the Exchange you will find that it is almost like a Tower of Babel. A large number of people are simultaneously shouting the names of different concerns and it is not possible to know as to who is interested in what. The volume of transactions that takes place is something colossal. A new class of youngsters have got into the market who themselves or whose family have made fabulous profits in the last three years and these youngsters think nothing of buying up the entire shares of a company. A bid of 25,000 or 50,000 shares has been a common thing in the market. If coal shares have gone up as a result of buying by one group of operators, then the other group extends its attention to cotton shares and a third to jute. No one stops to think about or study the intrinsic position of the company whose shares he is buying. They just descend like hungry wolves and devour all that they can lay their hands on. The result is that the prices of many shares have been forced up to a level which is almost equal or in some cases even lower than the return on government securities. How long can this go on God alone knows. The present market is not a market for shrewd speculators who always study the pros and cons of everything that they interest themselves in. The present market is for people who can rush in blindly and follow the current view. It is only such people who can make money."

I perfectly agree with the views expressed above. Take for instance some of the leading shares, say, Howrah, Irons, Steels, and Burakurs. According to the latest dividends paid by these companies the return on these

shares is approximately 1½, 4½, 2.5% and 2.5%. Some of the coal shares have gone up so much that the rise in them has discounted all possible future favourable factors.

One should therefore pause and take stock of the situation. This does not mean that one should be in a hurry to dispose of his holdings. But I would advise all shrewd investors to thoroughly examine the prospects and dividend paying capacity of each and every share.

(2) From now on till the budget is out of the way I expect a fluctuating market. No sharp rise or fall is expected unless the war situation takes a sudden turn. These expectations are, however, liable to be upset by the operations of that new class of operators to which I referred in my last week's gossip.

There is a Marwari saying that to a man who is born in the mouth of SHRAVAN everything appears green. This new class of operators, from the business point of view, was born in a period of unprecedent prosperity and easy money making. They have no idea that there is something called "Depression" when one is forced to sell one's holding for a mere song, that there are times when the industries that had been producing money start swallowing it back. They do not know that after the post-war boom of 1920 prices of many shares came down to ridiculously low figures. To give only one instance, the price of E. D. Sassoon United shares which sold up to Rs. 17 per share came down to only about a fourth of a rupee. But the man who has seen these ups and downs cannot go on buying shares blindly without paying any heed to the return and the future prospects of the security.

Returning to the Stock Exchange I find that a certain group of operators are playing a very profitable game to themselves but which will ultimately prove very dangerous for the small and uninformed operators. This group first buys up quietly a fair-sized block of shares in a particular concern and then starts tipping all and sundry both here and in other centres that it is good to buy this particular security. Nothing succeeds like success. As this group has been successful in pulling up prices of the securities recommended by them by the sheer weight of their purchases or due to favourable circumstances, the result is that many people now follow them blindly without waiting to examine the relative merits of the shares that they are buying. The large number of underbrokers and assistants who secure business from their clients pass on the tip to their clients and so the ball is set rolling. The group unloads its purchases at a handsome profit and then transfers its operations to another security. But as I have said before, the period of rising prices cannot go on indefinitely. Those who buy blindly will find that they will lose in one deal what they have made in ten.

Measures to Check Speculation. Speculation on a stock exchange cannot be absolutely abolished, but it can certainly be kept within reasonable

bounds if suitable measures are adopted. Some of these methods are as follows :—

It is often contended that speculation is the result of forward trading and the facilities of carry-over from one settlement to another, and therefore with a view to checking speculation forward trading should be abolished. But it must be recognised that those stock exchanges which do not permit forward trading are not also free from speculation. In spite of the fact that only cash business is permitted, transactions are not often completed within the time fixed and are carried over. Forward trading, as a matter of fact, is the essence of a stock exchange. What is needed is its control and not its total abolition. For a country like India with immense possibilities of industrial development, the provision of a free and wide market for industrial securities must be maintained to stimulate a continuous flow of fresh capital into industrial enterprises, and in order to achieve this the stock market facilities must be widened. Forward trading makes possible the existence of continuous market and therefore its abolition is not desirable.

It is necessary that a proper control should be exercised over stock exchanges by some governmental machinery such as a national investment board. The measures taken by government in the past have not solved this problem, and a permanent state machinery, which will watch the activities of the various stock exchange and take suitable measures to safeguard the interests of investors, is needed. The government machinery so set up will not only co-ordinate the activities of the various exchanges but it will also bring about permanent reforms in stock exchange practice.

At the Bombay Stock Exchange the most prolific source of speculation is the activity of a class of members of the Exchange who are not brokers in the real sense of the term. Some members, so-called brokers and mis-called jobbers, carry on what is known as *taraucani* business which is entirely of a parasitic nature. They rush in to buy or sell according as they find bona fide brokers trying to execute buying or selling orders. Their operations necessarily result in price movements almost always to the detriment of clients' buying or selling. These *taraucanicalas* hardly keep any outstanding business overnight and they continuously go on buying or selling at a small range of fluctuations. Their actions are nothing but gambling in differences. This state of affairs should be reformed. But as the volume of business at the present time does not warrant a permanent classification of members into brokers and jobbers, the members should declare at the beginning of each year whether they wish to act as brokers or both, and the stock exchange authorities must see that their decisions are strictly followed.

The non-existence of any system of margins makes possible for people of small means to trade on the market. It is therefore desirable that a system of margins should be introduced whereby every dealer should be required to deposit an initial amount with some authority, preferably the clearing house,

and the margin should not be allowed to fall below a certain percentage. A little concession in the matter of time may be allowed in the case of upcountry clients.

The system of blank transfers so rampant in the country should be properly regulated. The use of blank transfers affords an opportunity for further speculation. Under the present system the seller transfers to the buying broker a blank transfer form duly signed together with the scrip and the buyers do not get their shares registered in their own names at the company's office, as they intend to sell these shares again as soon as the market improves. In the present state of things it may not be desirable to abolish the system of blank transfers altogether, but their period of currency should be restricted. It must also be pointed out in this connection that the system of blank transfers is partly encouraged by the high rate of stamp duty on transfers. Therefore a reduction in the stamp duty may curtail to some extent the use of blank transfers.

Private compromise, though punishable under the rules of the Bombay Stock Exchange, is very common in Bombay and provides an encouragement to unhealthy speculation. On the Bombay Stock Exchange there exists a Defaulters' Committee, but the Committee seems to have no work. This laxity in the enforcement of rules further encourages reckless and irresponsible dealings on the stock exchange, as the members know that, if they overtrade, they have more to gain than to lose since losses have not to be paid in full and can be compromised. Such a compromise should not be permitted, and the rules should be rigidly enforced in order to remove unscrupulous defaulters from the market who take undue advantage of the market conditions.

Under the present rules of our exchanges, authorised clerks of members are not, of course, permitted to make bargains in their own names, but they are not prohibited from dealing for themselves. They can buy and sell on their own account through a member, in the name of a member and under his instructions. This leads to a serious abuse. For example, if a clerk has a large order to be executed in the market, he can first deal on his own account at the advantageous price and his employer or the client might be the victim. Such authorised clerks should not be allowed to do business for themselves.

To restrict the magnitude of speculation, it is also necessary that the list of securities should be widened and opportunities provided for a large number of investors. At the Bombay Stock Exchange, shares of only those companies can be traded in which keep a register in Bombay. This is not a very encouraging restriction. There is no reason why shares of companies having a register in various parts of India should not be permitted. This would widen the field of business and would reduce price fluctuations. In addition, deferred shares are by their very nature more speculative and they should therefore be removed from the forward list.

It is also sometimes suggested that a sales tax on all forward dealings may

be levied in order to check wild speculation. In order to provide additional facilities to investors, the number of shares should be increased by subdividing the high-denominational shares which are usually the favourites of speculators, because they can be easily cornered.

Finally it must be noted that most of the speculative business is financed by means of loans; and if a restriction is imposed on the granting of loans to speculators, there may be a check on wild speculation.

Characteristics of Indian Stock Exchanges.

Each Stock Exchange in India has its own peculiar characteristics. Broadly speaking, Bombay is venturesome and speculative, Calcutta is sober and calculative; and Madras is cautious and conservative.

Bombay Stock Exchange. The Bombay Stock Exchange is said to be the hot-bed of speculation. Why? Reasonable facilities for speculative transactions are a necessary and healthy part of the machinery of a Stock Exchange, which provides a free market where securities may be bought and sold to the best advantage and without undue delay. But the Bombay Stock Exchange provides too many facilities for reckless speculation, and these are as follows—

1. **Protection of Speculators** The rules of the Exchange dealing with corners and bear raids protect the bulls and bears and have encouraged excessive trading and speculation in the market. The Board of Directors have had the following powers of intervention in the normal operations of the market:—

- (a) Power to suspend the selling-out rule;
- (b) Power to suspend dealings in shares and securities subject to bear raids;
- (c) Power to suspend the buying-in rule;
- (d) Power to suspend dealings in shares and securities in which a corner has been effected and to fix prices at which settlement in such cases may be effected; and
- (e) Power to close the market in crises.

The possession of these powers by the Board has engendered in the operators—whether bulls or bears—a wholly unhealthy mentality, because they feel secure against the consequences of their own rashness and hence they tend to operate recklessly regardless of the resultant consequences both to the market and to the genuine investor.

It is clearly of the first importance that this mentality should be eradicated by eliminating from the organisation and constitution of the market the principle of intervention with a view to correcting difficult situations which result entirely from the internal operations of the market.

2. **Violability of Bargains.** This is another factor which has led to excessive speculation. A bargain once entered into in the market must be implemented regardless of consequences. On the Bombay Stock Exchange

bargains are not always inviolable, and the working of the principle of compromise to avoid default has been responsible for so much unhealthy speculation.

Compromise in any shape or form in order to avoid default should be prohibited under pain of severe penalties. If members begin to realise that the Board has no longer power to intervene between them and the consequences of their actions, they will in sheer self-preservation discard recklessness and conduct their business on more cautious and conservative lines.

3. **Leniency towards Defaulters.** Under the rules of the Exchange the defaulters have been leniently treated. Failure to fulfil contractual obligations not only to a fellow-member but also to a non-member should be followed by a declaration of default and a defaulter should be readmitted only on very strict terms, e.g. a member whose default has been brought about by speculation on his own account should not be readmitted under any circumstances.

4. **Travniwala:** The most prolific source of overtrading is the activity of a class of members of the Exchange who are not brokers in the real sense of the term—that is to say, they do not live on remuneration for the sale and purchase of shares on behalf of bonafide customers. These non-broker members, miscalled jobbers, carry on what is known as *taravni* business, which is entirely of a parasite nature. They rush in to buy or sell according as they find bona fide brokers trying to execute buying or selling orders. Their operations necessarily result in price movements almost always to the detriment of clients' buying or selling. The *taravniwala* is always an unnecessary obstruction to the fair execution of clientele business and often a toll-gatherer of a size incommensurate with the risks he runs. Besides, as all the operations of these dealers are essentially for a settlement of differences, with absolutely no intention to pay for a single share purchased or deliver a single share sold, the size of their operations has no reference to the value of the stocks sold or purchased, and consequently the operations are limited only to the avidity of the dealers.

It is therefore suggested that all members of the Stock Exchange should be divided into jobbers and brokers.

5. **No System of Margins.** Another reason for overtrading in the Bombay market has been the lack of a sense of values as represented by purchases and sales. As a remedy the introduction of a system of margins has been suggested whereby every broker would be required to submit every day a list of the transactions at the overnight closing time in order to prove that he had the requisite margin from his clients. A mere initial margin should not be enough, it must be kept up to the required level as the transactions increase, with a slight concession in respect of time to up-country clients. The same restrictions should apply to brokers or firms who deal on their own account.

6. **Use of Blank Transfers.** Another facility which favours speculation is the extensive use of blank transfers. The use of these should be strictly limited. But the present stamp duty on transfers is so high that it encourages the use of blank transfers.

7. **Longer Settlements.** Bombay has monthly settlements in connection with forward business. The longer the settlements are apart the more inducement there is for speculation. It is suggested that settlements should be fortnightly instead of monthly.

8. **No Minimum Brokerage.** The absence of a minimum scale of brokerage enables a powerful operator to set off one broker against another and get his business put through for next to nothing. This is partly responsible for overtrading. A minimum scale of brokerage should therefore be fixed.

9. **Unlimited Business Hours.** The unlimited time allowed for business encourages speculation. A readjustment of the hours of working and holidays is suggested. A four-hours business day may be enough.

10. **Sub-Brokers** This is another evil which encourages excessive speculation and must be restricted.

11. **Tradition.** In the past many wealthy persons of Bombay have acquired wealth through speculation; and therefore in the minds of the general public speculation is a royal road to fortune.

Calcutta Stock Exchange. The Calcutta Stock Market is known to have done its business in sober and calculative manner. There has been no forward trading in the market, business being confined only to cash account, and this fact has been responsible for the absence of wild speculation there.

It should not, however, be understood that there is absolutely no speculation in Calcutta. There has been speculation but not wild speculation. The affairs of the Exchange have been well administered by the authorities. Calcutta is younger than Bombay and has learnt a useful lesson from the bitter experience and colossal losses of the latter. Of late, however, Calcutta is also tending towards the rock of disastrous speculation.

Madras Stock Exchange. This is the youngest of the three principal stock markets in India, having been established only in 1937. It is run on very cautious and conservative lines; and therefore speculation is almost nil there. Only cash business is permitted and the days of delivery are only three. Thus there is absolutely no scope for the activities of speculators.

Fluctuations in Security Prices

A person, who wishes to operate in stock exchange securities, must be able to judge when to buy them and when to sell them. This can be done only when he understands the factors that influence their prices. Many factors are liable for price fluctuations.

"The winds that play upon stock exchange markets are as varying and as those that blow upon the ocean. They are frequently just as disturbing. By markets we mean the level of prices at any one time in existence."

These price levels are extremely sensitive and susceptible to all kinds of influences. For days, barometrically speaking, the needle will point to 'Fair' and trading on the floor of the 'House' will proceed along quiet and uneventful lines. Sooner or later, however, the cloud little larger than a man's hand appears, to be followed before long by wind and storm. Even before members are quite aware of it, they are in the midst of a veritable squall. Often news, good or bad, is dramatic, when price movements are violent. In this case the result is of an unsettling character. Repercussions are felt throughout the whole market, and stocks and shares far removed from the actual scene of the disturbance are affected." (F. L. Armetrong: *The Book of the Stock Exchange*)

The prices of securities, like those of other commodities, are mainly governed by the law of demand and supply. An increase in demand or decrease in supply would always tend to raise the price, while a decrease in demand or an increase in supply would lead to a fall in prices. The supply of stock exchange securities is, however, limited, it cannot be increased by accelerating production. The following are the principal factors that influence price fluctuations in security prices, because they have a bearing on the demand and supply of securities :—

1. **Money Rates** The value of money, by which is meant the rate of interest at which money can be borrowed, exercises a powerful influence on security prices. A decline in short-term interest rates tends to increase the activities of speculators, who take advantage of the lower rate of interest and borrow money for purchasing securities which enable them to make a good profit. At times when the rate of interest has fallen, an added impetus is noticed in security dealings, which in turn leads to a rise in their prices. When, on the other hand, money is dear and scarce, the securities fall in price.

2. **Currency Inflation.** Currency inflation leading to surplus purchasing power in the hands of the public has vitally affected security prices in recent years. More money means greater demand, and greater demand leads to soaring prices.

3. **Trade Activity.** Trade booms and slumps affect security prices to a considerable extent. During a boom prices of all securities tend to move up as has been fully demonstrated during the last few years. The experience of the recent war indicates that a rise in security prices tends to coincide with a period of business prosperity. In a period of depression the tendency to dullness prevails in all markets, and there is an all-round curtailment of production. The declining commodity prices lead to heavy losses and the shaking of public confidence. There is a general pessimistic outlook, and this brings about a general fall in security prices.

4. **Political Situation.** War is a mighty upheaval that brings about changes in all spheres of business activity. The stock exchange cannot be free from its consequences. In war time the government influence is so dominant

that it governs the course of prices to the exclusion of every other factor. Values change all round when fear grips the market and politics displaces business at the steering wheel. This fact has been well illustrated by the experience of the recent war when security prices widely fluctuated from time to time. Throughout the war period, the reverses of the Allied nations brought about a setback in prices, and their advancement and victories caused prices to improve.

It is not only the war that affects the minds of stock exchange operators, but other political developments both at home and abroad also bring about price changes. On many occasions during the last twenty years, stock market prices in this country have been vitally affected by political changes. The Congress struggle for freedom has had its due share in this direction.

5. **State Policy.** Any state action that affects the trade and industry of the country is bound to have a corresponding effect on security prices. Such government actions may consist of imposition of new taxes, grant of protection, price control, nationalisation, introduction of prohibition, control of public utility concerns, etc.

6. **Technical Position.** The technical position of a particular security refers to the volume of speculation existing at any time in that security. When the speculative purchases made by bull operators in any particular security exceed the speculative sales, there is said to be an *overbought* position; and when the speculative sales of a certain security exceed its speculative purchases, there is an *oversold* position. The overbought or oversold position is the technical position. An overbought position is bound to lead to a fall in prices and an oversold position must stimulate prices. This is a subtle factor influencing security prices.

7. **Market Psychology.** The market psychology is an important factor as regards price fluctuations. At one time one scrip is favoured while at another time another security comes into the limelight simply because the market operators think so. There may not be any particular reason for the choice. Market people are like sheep, and sentiment is infectious. Very often, sentiment, influenced by vague rumours, rules the market. Prices are determined not by any intrinsic factors but by the whims of the operators.

8. **Intrinsic Position.** The prices of company shares may depend to a certain extent upon their intrinsic position, namely, the result of their working and their financial strength as disclosed by their published accounts. The amounts of profit made, depreciation provided, reserves created and dividends declared, are things that affect the share prices.

9. **Vagaries of London and New York.** All the stock markets of the world are interdependent. Should anything happen to disturb the course of security prices on the London or New York Stock Exchanges, it is bound to have some influence on Indian stock exchange prices.

10. **Press Opinion.** The power of the press is proverbial. Newspapers

and periodicals devote a special column to commercial and financial news and views which are looked upon by dealers with impatience, as they all contribute to the making up of prices. In addition, certain newspapers employ trained writers to review the conditions on the stock exchanges, and frequently tips are thrown out to the readers. If a newspaper has established a reputation in market circles, its opinion exerts some influence on price movements.

11. **Miscellaneous.** Stated above are some of the principal factors that influence security prices; but they are not all. There are many more things that may affect the judgment of market operators as regards prices.

London Stock Exchange

For more than one hundred and fifty years, the London Stock Exchange has played a very important part in world finance, and, during that time, it has had considerable influence upon the industrial affairs of Great Britain. To-day, a huge volume of business is transacted on the vast floor of the old building which stands in the shadow of the Bank of England. Regular dealings are made in over 10,000 different securities, the recorded transactions of which appear in the Stock Exchange Official Lists. These daily transactions may range from one in Government stock involving millions of money to a deal in shares involving but a few pounds.

Popular misconceptions have always existed regarding the real function of the London Stock Exchange. But this is no centre for the reckless gambler any more than it is a kind of club for rich business men in the City of London. It is simply a free market, in which the sale and transfer of investments is governed by a strict code of rules and regulations, designed not only to protect the members themselves but to safeguard the public against fraud.

On the Stock Exchange, as in any other market, buyers and sellers are brought together and deals are conducted quickly and efficiently. Anyone, whether he is a large or small investor, may do business with a duly elected broker member of the Stock Exchange.

History of the Exchange. Dealings in stocks and shares probably began in the old time coffee houses of London during the seventeenth century. Business was done at informal meetings of brokers with a few stocks of such famous trading concerns as the East India Company and the Hudson Bay Company. Change Alley, not far from the present Stock Exchange, was the favourite centre of these early financial transactions.

In the reign of William III (1689-1702), a permanent national debt was established as the best means of centralising Britain's financial resources for State expenditure. From that time onwards, stock-broking became an important and specialised profession. Moreover, as British adventurers and traders opened up new markets in various parts of the world, London became the centre of investment. Money was soon pouring into the City from eager investors overseas as well as at home.

Chang's Alley continued to serve the brokers and dealers until the year 1801, when the great increase in investment necessitated a special Stock Exchange building. This was opened in Capel Court, and, though enlarged and altered some fifty years later, has since remained the permanent home of the London Stock Exchange.

The Stock Exchange is an unincorporated company, constituted under a deed of settlement dating from 1602 and amended in 1875. Before March 1945, the management and finances of the undertaking were in the hands of the trustees and managers representing and elected by the proprietors for a period of five years, while the rules and regulations governing the members and conditions of business were in the hands of the Committee for General Purposes elected annually by members of the Stock Exchange.

On 25th March, 1945, the present Council of the Stock Exchange came into being, amalgamating in effect the powers of the trustees and managers and of the Committee for General Purposes. The trustees and managers became foundation members of the Council subject to the same conditions of re-election as heretofore and the members of the Committee for General Purposes became the ordinary members of the Council and one-third of their number are liable for re-election annually.

Membership Qualifications. To be elected a member of the London Stock Exchange is still regarded as something of a privilege; in many families it is a tradition handed down from father to son. To become a member of the Stock Exchange costs money. Under normal conditions, before applying for membership, the applicant will have served four years as a clerk in the House, and if elected, will have to pay 300 guineas entrance fee, a subscription of 50 guineas and to purchase one Stock Exchange share. An applicant who has not served such an apprenticeship will, if selected, have to pay 600 guineas entrance fee, 100 guineas subscription, and to purchase three Stock Exchange shares. Applicants in either case have to purchase a nomination. The cost of Stock Exchange shares is approximately £120 and of a nomination £400.

A member of the Stock Exchange should be British-born, must be twenty-one years of age, and may not engage in any other form of business. He is subject to re-election annually, a privilege which the Council have the right at their absolute discretion to grant or withhold.

Brokers and Jobbers. All the members of the Stock Exchange are divided into brokers or jobbers. The brokers buy and sell shares on behalf of their clients, the general public, and their income is derived from the brokerage or commission, charged on every transaction. Commission rates chargeable on all classes of securities—and they vary accordingly—are fixed by the Council.

Jobbers are the men who actually buy and sell the securities; they work inside the House all the time and they may not do business except with a broker or a fellow jobber. At the opening of business each day, the jobbers are to be found at their customary pitches or "stands" awaiting the orders of the brokers.

These dealers are the key-men of the market and it is around them that all business on the Stock Exchange revolves. Each is a specialist in certain types of securities, and the floor of the House, is, by long custom, divided up into the various markets. There are markets in Government securities, foreign bonds, bank and insurance stocks tin, rubber, gold-mining shares, and so on.

When a broker wishes to deal in a certain share for his client he will approach one of the jobbers in the particular market and, without disclosing whether he is a buyer or a seller, ask the price. The jobber quotes his buying and selling price, and must be prepared to deal either way. The margin between these two prices varies according to the current state of the market. This margin constitutes what is known as the jobber's "turn" from which he obtains his livelihood.

There is, of course, much keen competition among the jobbers, which tends to keep the margin of their "turn" narrow in securities, in which there is a free market. There is a highly skilled profession and one that requires wide knowledge of the securities that come within their range as well as a keen appreciation of market influences at any given time. That is why an efficient jobber must always be a speculator.

Conduct of Business A remarkable feature of Stock Exchange practice is that neither the broker nor the jobber signs anything when a transaction is made between them. Both parties merely make a note of the price and the number of shares bought or sold, and that is all. But from that moment the shares have changed hands and the transaction is binding.

Every morning in the selling room below the Stock Exchange, the clerks of the brokers and jobbers meet to check the bargains made verbally in the House on the previous day. This is to make sure that no mistakes have been made before the machinery for the transfer of the shares is put into operation. But errors seldom occur.

Business on the London Stock Exchange is either on a cash basis or for fortnightly accounts. The system of account dealing makes for more orderly marketing as the client knows exactly when the payment for a delivery of his securities will be required and makes possible the organisation of the Settlement Department whereby transactions are cleared and the work in members' offices largely reduced and the service to the public simplified and expedited. The existence of fortnightly accounts enables the speculator to make a quick profit in active markets without putting up any money.

Only members and their admitted clerks may enter the House, although permission is granted to privileged visitors under suitable escort. There are uniformed attendants, known as "waiters", at all the entrances to see that no unauthorised person tries to make an entry. A "waiter" will call any member from within if a client wishes to speak with him outside, though most business between brokers and the public is done at their offices in buildings nearby.

At times when the House itself is closed—as, for example, after the

declaration of war in September, 1939—business is carried on in the normal way outside in Throgmorton Street. This narrow thoroughfare which runs down beside the Stock Exchange is just "the street" to all members; it is one of the liveliest corners of the City of London with informal meetings of brokers, jobbers and clients going on nearly all day long. Much the same atmosphere must have prevailed in Change Alley well over a century ago.

Note.—On all the Indian stock exchanges there is no classification of members into brokers and jobbers. All members are called brokers, but they are free to act as both, that is to say, they can do both classes of business—broking as well as jobbing. This is due to the fact that membership of our stock exchanges is not so wide nor is the volume of business passing so large, as in the case of the London Stock Exchange where members are divided into brokers and jobbers. If some of the members of an Indian stock exchange were to confine themselves only to jobbing, the profit would not be worth the risk on account of the smaller margin of profit. It is therefore in the interest of the members themselves that they are not divided into brokers and jobbers.

It is true that from the point of view of the public it is desirable to have two distinct classes of stock exchange members, namely, brokers and jobbers, because in that case the brokers would become disinterested middlemen and would inspire confidence in the minds of their clients. A broker as broker would be more reliable than when he is both. It is generally admitted that this change is desirable, but it does not appear to be feasible under the present circumstances for two reasons. Firstly, the volume of business transacted is not sufficient and secondly most of the business is done on account of members themselves.

Test Questions

1. What is the utility and importance of a Stock Exchange? Explain: Carrying over, Jobbers, bears, cantage, and corner. (*Bombay B. Com. 1937*).
2. Discuss the organisation of the Native Stock and Share Brokers' Association, Bombay, with a view to throwing light on what you consider its weak points. (*Bombay B. Com. 1938*).
3. Briefly describe the organisation and working of any stock exchange. (*Bombay B. Com. 1946*).
4. Explain the service which the speculator performs as a risk bearer. Illustrate the effect of his operations by examples of the stock Exchange or the Commodity Markets. (*Bombay B. Com. 1935*).
5. An investor, living in Agra, desires to purchase five deferred shares of the Tata Iron & Steel Co., Ltd. Write a letter to him, giving detail of the procedure to be followed. (*Agra B. Com. 1946*).
6. Explain: Put option, Carrying over, Contango, Corner and Bears as used in the stock exchange. (*Agra B. Com. 1942*).
7. Explain and illustrate the following stock exchange terms: Cornering; Sagging; Bull-rigging; c.d.c.r. Quotation. (*Agra B. Com. 1945*).

8. Discuss the beneficial as well as adverse influences of the Stock and Produce Exchanges upon industry and trade. (*Agra B. Com. 1943*).

9. Estimate clearly the functions and services of the broker and the jobber in the London Stock Exchange. Would it be advisable to adopt this bifurcation for Indian Exchanges? (*Agra B. Com. 1940*).

10. Examine briefly the principal factors that govern the prices of stock exchange securities. (*Agra B. Com. 1944*).

11. How do the leading exchanges of the world deal with the evil of speculation? What steps have been taken to deal with it in the Bombay Share Bazar? (*Bombay B. Com. 1939*).

12. What sources of information are available to a person desiring to invest his money in the industrial securities of a concern? How far does this information enable him to make investment on a rational basis?

(*Bombay B. Com. 1941*).

13. A person wishes to buy five ordinary shares of the Tata Iron & Steel Co., Ltd. Trace in detail the course of events that will make him the owner of these shares.

(*Bombay B. Com. 1944*)

14. Is it desirable to check speculation on the stock exchange? Is it practicable?

(*Bombay B. Com. 1944*).

15. What is the official list of a stock exchange? What is the purpose of listing regulations? What is option Business?

(*Bombay B. Com. 1946*).

16. Distinguish between speculation and gambling.

(*Rajputana B. Com. 1949*).

CHAPTER XIII

RATIONALIZATION AND SCIENTIFIC MANAGEMENT

For some years now, one of the guiding principles of economic development has been rationalization. There is rationalization of factories and of whole branches of industry. Attempts are made to introduce it in the distribution of goods, in agriculture, in public and private administration, in the economy of whole countries and even of the whole world. At the same time methods of bringing it into the narrower sphere of domestic economy are sought.

To be rational is to act according to reason, and therefore rationalization must have existed ever since the beginning of industry. Thus most of the methods now included in the term rationalization are not new, at least in principle. What is new is their systematic use, the increased pace of their application and also certain methods. The attention diverted to those methods has been so common and the success achieved has been so spectacular that it has come to be regarded as entirely a new phenomenon which began towards the end of the first world war, while in fact only the movement was accelerated by some special conditions arising out of the war.

First of these conditions was the shortage of things which was very keenly felt during and after the war. The result was to make a systematic attempt to make the most of the available resources. In Germany particularly, this policy of economy was applied rigorously. Devices were found to substitute new arrangements for shortage of labour. Thus the evolution of a new technique was accelerated. The new demands which were made after the war by powerful labour organisations about reduction in hours and increased wages also pointed the way towards new arrangements whereby to reduce the labour costs. Besides, the depression which set in after the war gave a new fillip to the movement inasmuch as efforts were made to reduce costs of production, and therefore to reorganise equipment and technique. Finally currency disturbances also had their part to play.

Thus manual work was replaced by mechanical processes in many new fields of manufacture, and the industrial technique was completely revolutionised by the progress in electrical, engineering and chemical industries. The types and patterns had been simplified, and the varieties were reduced. There was a tendency towards uniformity in size, shape and quality of many articles based on certain standards. In other words the movement towards simplification of varieties, standardization of materials and products, use of elaborate machinery in place of hand labour as well as the combination of the different firms'

in the industry with a view to securing plant specialization, the closing down of uneconomical firms, reduction of the overhead costs and economy in selling was accelerated. The most important advancement made towards rationalization consisted in the new enthusiasm and interest in industrial research. It was in this field of industrial research that the questions of time, motion and fatigue study were taken up and suitable methods have been developed to tackle the different problems that have arisen in that connection. The analysis of individual work was followed together with the time of the whole process, and the new progress was made in the application of the principle of division of labour. Thus rationalization is a scientific scheme of cost reduction by putting reason into industry.

In what, then, does this rationalization movement, so characteristic of the present age, consist? In the systematic effort to get the most out of the resources—labour and materials—employed in the various economic activities, rationalization means that instead of traditional processes, established routine, empirical rules, and improvisation, use is made of methods that are the fruits of patient scientific study and aims at the optimum adjustment of means to ends, thus, securing that every effort produces the maximum useful results. In the words of the World Economic Conference of 1927, it refers to "the method of technique and of organization designed to secure the minimum of waste, either of efforts or of material."

The International Labour Organisation adopted the following definitions:

(a) Rationalization in general is any reform tending to replace habitual, antiquated practices by means or methods based on systematic reasoning.

(b) Rationalization in the narrowest sense is any reform of an undertaking, administration or other service, public or private, tending to replace habitual, antiquated practices by means or methods based on systematic reasoning.

(c) Rationalization in a wider sense is a reform which takes a group of business undertakings as a unit and tends to reduce waste and loss due to unbridled competition by concerted action based on systematic reason.

(d) Rationalization in the widest sense is a reform tending to apply means and methods based on systematic reasoning to the collective activities of the large economic and social groups.

It aims at elimination of waste in cost of production, elimination of competition, cooperation among producers, and in general avoidance of the evils of extreme individualism without creating the evils of monopoly. It is a technique which seeks to remove the evils of defective business organisation, inadequate and unsatisfactory technical equipment, both in personnel and machinery, obsolete marketing methods, overcapitalization and excessive overhead charges, results of lethargy and thoughtlessness, mistakes and miscalculations.

The aim of the industrialist is to have maximum profit, and his success depends upon (1) producing with minimum of cost and maximum of output,

(2) efficiency of men working on different processes in turning out the largest quantity of products of a given type (standardisation), and (3) the efficiency of management in preventing waste and unnecessary expenditure. Rationalization aims at achieving the above objects by adopting different methods.

The methods of rationalization to achieve its aims have been divided into two principal groups:—

- (i) Scientific Management and
- (ii) Measures of rationalization not directly connected with labour.

Scientific Management

Scientific management owes its inception to Dr. F. W. Taylor, an American engineer, who published his principles of scientific management in 1911. It deals with systematic organisation of production. The method is to determine the best ways of doing particular jobs, eliminating all unnecessary efforts and reducing the worker's fatigue to an absolute minimum.

Taylor's work centered round three cardinal principles, namely, time study, motion study and fatigue study. By an analysis of time, motion and fatigue almost every manufacturing operation may be split up into several elemental parts. The number of movements involved are minimised, the motions involved are carefully analysed, charts prepared for the most efficient motions and the advantages of specialisation and division of labour fully exploited, so that the workmen might achieve maximum of work, efficiency and output with the minimum of effort, with the maximum of rest and spare time and with the maximum wages.

Scientific management consists in devising methods of securing the maximum productivity from each man and each machine with the minimum waste of either effort or material or time. But the productivity of man cannot be maximised unless a man is given a job for which he is best suited according to his aptitude. The best standard method of doing the work and the minimum or the standard time to complete it are found out in advance, the requisite training to do the work is provided for, and above all an impetus in the form of bonus and extra wages to those who complete their work within the specified time is given.

Many scientific instruments are used and many complicated and delicate recordings taken for studying the psychology of the worker, the working environment and the motions involved in work, as all those factors have been found to be fundamental in determining work, efficiency and output. As a result of such study, all work is planned in detail beforehand. Every operation is guided scientifically. Further scientific management is accompanied by the introduction of functional foremanship, under which the same work in all departments is placed in charge of one foreman who is a specialist in one kind of work, while another work is entrusted to the supervision of another foreman who is a specialist in that work, and so on. The underlying idea is that one man is made responsible for one or as few functions as possible. The workman therefore

will have to take orders from different persons for different functions. This organisation is called '*functional management*' as opposed to the old-fashioned '*line*' organisation.

The line system is a monarchical system, in which the work of the concern is subdivided into departments and the distribution of authority is on the military principle. There are several self-contained departments, each with a sub-manager, who is responsible to the general manager. Under each sub-manager there may be further staff, arranged in descending order of authority. It generally secures a certain amount of efficiency, speed and certainty in work, but there are certain disadvantages too. In the first place, the system depends upon the ability of a single individual. Secondly, it cannot be expanded too easily, and thirdly the organisation of work in one department may be quite different from the organisation of work in another department; and this lack of coordination between different departments may result in waste and inefficiency. Finally the line system places greater emphasis upon discipline and not so much upon productive efficiency.

However, the combined line and staff system is an effort to strike a balance between the functional and the line systems. Discipline is maintained on the basis of the line system, but efficiency is developed by having advisory staff, who will advise the management on all problems of technical efficiency. The purpose of the staff is to give information, advice and practical facilities to executive officers. For example, a special staff may advise the general and another the sales manager, while a third may collect information and give advice on market research.

Thus scientific management is characterised by replacing guess work and traditional methods of doing business by methods based on systematic knowledge and research. Instead of the engagement and discharge of a worker by the process of trial and error, the qualities required by him for the most successful performance of his work are ascertained by a systematic enquiry. Instead of being allowed to pick up the methods of his work as best as he can, a worker receives a careful training in the most suitable working methods revealed by previous investigations. Instead of using the traditional form, weight or quality of tools, he is provided with those which research has shown to be most suited to the conditions of his work. Instead of payment being made to the worker on some traditional basis, efforts are made to devise some scheme which will serve as an incentive to production. Instead of each member of the management from the general manager down to the foreman being burdened with a vast number of multifarious functions to perform, he is enjoined to specialise in a smaller number of management duties.

Similarly machines are kept in proper repairs and tools are of the best shape, size and pattern. Installation of the best available machinery and tools, study of materials of production, and the determination of most effective speed of the

machines, rearrangement of material equipment to allow continuous straight-line production and a careful time, motion, and fatigue study are some of the other features of scientific management.

Scientific management, therefore, seeks to lower costs of production through increased and better application of technology to industry, through increased specialisation of management, through better location of individual responsibility and through better methods of wage payment. A separate planning department with its able and experienced manager and other experts and a separate production department with its difference sections under the control of several bosses are of immenso help in securing the above objects.

Scientific management is a part and parcel of rationalization. The scientific management connotes the best organisation of one concern considered as one unit. It is also a scheme of waste reduction and looks more to the technical side of industry; whereas in rationalization more attention is paid to the economic side of the business. Moreover scientific management may not usually lead to big business but some form of combination is the usual feature of any scheme of rationalization.

Measures of rationalization not connected with labour

These comprehend all those measures that can, on grounds of systematic reasoning, be recommended for systematic adoption by an industry for improving its technique, its management and its finances.

Reorganisation is one of the measures that may increase technical efficiency effect economy in cost of production, eliminate waste, and reduce overhead costs. The problem of reorganisation is resolved into three heads—merger, modernisation and management.

Rationalization is of course associated with business on a large scale. It therefore involves amalgamation, integration and modernisation with the object of elimination waste. Production is concentrated in several modernised plants, wasteful duplication of efforts is avoided and uneconomic, antiquated units are closed down. It further aims at regulation output so that demand and supply are properly adjusted and prices are kept stable. A collective control of industry is instituted. Thus it seeks to bring the isolated, uncoordinated, self-controlled and self-contained units in the industry to the path of co-operation in the interests of the industry as a whole. The industrialists are expected to cultivate a new spirit and a fresh vision, so that a new sense of responsibility and public service emerges. There is a general desire to see the collective action in the interest of economy, efficiency and stability primarily to benefit the consuming public, so that the policy of price maintenance gives place to price reduction.

Broadly speaking, rationalisation is the bringing of the whole of an industry under intelligent direction and administration. It implies a conception of industrial organisation and control radically different from that which prevailed in the last century. It implies a conception of industry as an organic body with each separate establishment as a corporate part of the whole, no

longer expending energy in internecine conflict, but working together to a common policy and programme laid down by a directorate in whom absolutely authority over the industry as a whole has been reposed. Regarded aggressively, it implies an industry presenting a united front to the workers, carriers and consumers of its goods. Regarded constructively, it implies the organisation of an industry as a corporate whole in such manner as to eliminate friction, waste and slip to bring the technique and machinery of all establishments to the level of the best, and most of all to order the capacity, output, selling activities, and prices of the industry as a whole in accordance with what are deemed to be the present and future needs of the market.

Advantages. It is calculated to secure (a) to the community greater stability and higher standard of life, (b) to the consumer lower prices and better goods, and (c) to the producers higher and sturdier remuneration to be equitably distributed among them. It secures maximum labour efficiency. Waste of raw material and human effort is avoided. Distribution of goods is simplified: unnecessary cross freights, burdensome financial charges and useless interposition of middlemen are avoided. It leads to better research facilities and pooling of scientific, technical and business knowledge with which comes not only greater amount of profit for the manufacturer but also a healthier commercial atmosphere in society. It leads to big business units which are in a position to raise capital at low rate of interest. The huge financial resources make it possible for each industry to spend more on research and modern plants and employ better brains.

Rationalization measures depend for their success on more than the routine application of abstract schemes and mechanical principles—above all, on mutual good understanding and co-operation between employers and workers. The following are some of the main recommendations on rationalization made by the Bombay Textile Labour Enquiry Committee :—

1. It is eminently desirable that all the three parties to be benefited by rationalization, namely, the employers, the workers and the state as representing the consumers should co-operate in facilitating its smooth working.

2. It must be realised above all that the co-operation of employers and workers is vital to the success of rationalization.

3. If the industry is to prosper, workers must be taken into confidence and earnest endeavours should be made to remove their just apprehensions.

4. The essence of the success of any efficiency scheme is that it should be launched with the co-operation of those who have to work it. This must as far as possible be done after mutual consultation and after securing the best technical advice available.

Dangers. The first and foremost danger is the price policy of the rationalized industry. In spite of the claim that rationalization means lower prices, there is always a danger that monopoly prices may be charged by the industrialists who may pursue an anti-social policy and mitigate the joint

influences of supply and demand by restricting the supply of a commodity. The only remedy to solve the problem is the public legislation to regulate such industries. Moreover, the supply of suitable leaders and captains of industry is going to be a serious problem of rationalized industries.

Another serious danger of rationalization is that it will lead to unemployment. Rationalization aims at the increased productivity per worker through a rapid technical advance. But this technical progress has increased unemployment as happened in Germany. Moreover, the integration of industries and standardization of products may produce adverse effects on employment. But this does not mean that rationalization will always lead to unemployment. With the increased habit of investment and greater diffusion of education and mobility of labour, in the long run, there will be no unemployment excepting some temporary maladjustment.

Rationalization differs fundamentally from nationalization on the question of who shall be in control. Rationalization presupposes the retention, with no radical change, of the capitalist order. The ultimate ownership, control and management of the industry is vested, not in a democratic electorate of all those engaged in the industry and not in government department, but in the shareholders and other financiers of the combined units. Schemes for the increasing participation of labourers with the internal management and in the profits of the undertaking by means of works committees, workmen's representatives on the board and schemes of profit-sharing and co-partnership do not alter this fact. It is a recognised fact that rationalization can never prove an alternative to nationalization, but it should be welcomed during this period of private ownership so long as it would lead to improvement in the efficiency of industry and to the raising of the standard of living of the people.

Rationalization in India

Rationalization in Indian industries has not been carried to any great extent and the state of affairs in this respect remains extremely unsatisfactory. Excepting in a few stray and individual cases, no systematic efforts have been made to rationalize production. In most cases, selection and recruitment of our factory workers is still in the hands of the jobber—a system which is notorious for its evils and malpractices. We cannot boast of any organised attempts at proper training of the workers, and most of the Indian factory workers are still fresh from the villages—entirely unskilled and illiterate, the result being high labour turnover and absenteeism. Arrangement of premises, lighting and ventilation reminds us of our backward conditions. Plant and machinery are often out of date and obsolete; production units often too small and inefficient. There is waste of materials and equipment; no proper utilization of by-products; and industrial research is conspicuous by its absence. Any attempts towards rationalization that have been made in Indian industries may be seen below.

Cement industry. This industry is of recent growth in India, and very

soon after its beginning, the industry was suffering from internal competition, so much so that its very existence was threatened. In 1930, the Cement Marketing Company of India was floated, and this company was entrusted with the task of selling the total output of the members at economic prices. This was the first attempt. Each member factory is assigned a definite quota to produce of standard specification. Freights are arranged with different railways, cross freights are avoided as far as possible, and markets have been zoned for various brands of cement. The Company has thus been able to eliminate internal competition, reduce transport charges, avoid overproduction, increase demand, and provide better service and lower price to the consumer. In 1936, another step was taken whereby ten cement factories were amalgamated into one and were registered under the name of Associated Cement Companies, Ltd. In 1941, yet another step was taken and an agreement was reached between A. C. C. and the Dalma group of companies, whereby the internal competition was further restricted.

Sugar Industry. The growth of this industry has been very rapid during the last 15 years, but this rapid development left certain weaknesses in its growth. Sugar Marketing Board was formed to eliminate competition, but owing to the apathy and indifference of individual factories the organisation failed in its objects. Since 1938, the Sugar Syndicate has been formed, and there is stricter government control over production and distribution.

Jute Industry. Rationalization in the jute industry has taken the form of restriction of output. In order to meet falling prices and demand, the mills agreed to work 54 hours in 1929 was followed by a complete stoppage of work for three weeks in 1930. Ultimately 40 hours a week and sealing of 15% of the looms for the members of the Jute Mills Association was agreed in 1932. The scheme could not continue for long, the sealed looms were released and the agreement came to a close in 1936. In 1940, a Jute Conference was convened and it was agreed to compulsorily restrict jute acreage with the support of the government.

Cotton Industry. The Cotton industry is the biggest Indian owned and managed industry in India. The industry was not in a flourishing condition before the war. Large stocks had accumulated, and several mills were running at a loss. Internal competition had become serious. It was in 1936 that an effort towards rationalization of the industry was made, and a scheme for a merger was put forward. The scheme was torpedoed by the opposition of a few managing agents and vested interests. In 1941, the Bombay Textile Labour Enquiry Committee again recommended rationalization for the industry. Nothing, however, came out. The war gave a fillip to the industry and losing concerns began to pay high dividends. There was cloth famine. In 1945 it was the government which enforced rationalization upon the textile industry. The Textile Industry (Rationalization of Production) order was enforced with a view to increasing production of utility cloth. The number of

varieties were limited. Mills were required to devote 90% of their civilian capacity to production of utility cloth, and uniformity of quality of production was also required.

Engineering Industry. In this industry rationalization has taken the form of the introduction of new measures of efficiency accompanied by reduction in number of workers. In the Iron and Steel Works at Jamshedpur, production has increased per unit on account of introduction of labour-saving devices, increase in wages, extra bonuses, and necessary rest-pauses. In Agricola, production has considerably increased on account of introduction of piece-wage system. In the piece-work system the machine hour record is pitched up to such a high level that earning of appreciable bonuses is usual. Similarly, in the Indian Tin Plate Company, production has increased uniformly and considerably on account of this intensification. It is, however, in the Cable industry that intensification has been at its worst. While production has increased by over 250 per cent, operatives have been reduced to half. But in the majority of these establishments there has been intensification of labour for which workers have not obtained benefits through reasonable increases of wages rates, while necessary rest-pauses are limited only to small sections of the labour force.

This rapid review of the stray attempts at rationalization in Indian industries shows at once that they at present exist on a precarious foundation. It is only the cement industry which presents a rudimentary form of rationalization. Some of our major industries are in a chaotic condition. It is clearly evident that we have failed to keep pace with other important countries of the world. Our industries are still organised on individualistic lines. Indian enterprise still shows lack of ingenuity and foresight. At present the minds of our industrialists are focussed only on the manufacturing costs, market prices for similar articles, and the maximum profits that could be derived from the sale of their goods on the merits of present abnormal demand. We may no doubt pull on without danger so long as the present demand lasts. But, as soon as transport facilities by sea, rail, road and air become easy, these industries will have to face an unprecedented and planned competition from foreign countries.

It is urgently essential, therefore, that our industries should be rationalised. Our industrialists must know that their present fortunes will not continue to favour them for ever. In order to save us from the economic ruin that would otherwise overtake us, we must reorganise our industries. Our industrial organisation needs a thorough overhaul. Rationalization measures must be applied, overhead expenses must be curtailed, individual rivalry must be stopped and distribution of products should be brought up-to-date. Inefficient units of production must be discarded and closed. Greater attention must be paid to human factor to eliminate high labour turnover and absenteeism, to bring about stable factory conditions and to secure harmonious relationship between capital and labour.

Test Questions

1. What is "Rationalisation"? Discuss the problem of its application to Indian industries. *(Bombay B. Com. 1947)*
 2. What do you understand by Scientific Management? Is it different from Rationalisation? Explain clearly.
 3. Discuss the principles underlying Scientific Management. *(Bombay B. Com. 1947)*
 4. Explain in detail the 'line' type of organisation. In what way is the line and staff an improvement? *(Bombay B. Com. 1945)*
 5. 'Scientific management involves in its essence a complete mental revolution on the part of the workmen and an equally complete revolution on the part of those on the management side.' Discuss *(Agra B. Com. 1942)*
 6. Write a critical note on Rationalization with special reference to Indian industries. *(Agra B. Com. 1946)*
 7. Of two large-scale organisations, one follows the 'line' principle and the other is organised on the 'line and staff' principle. Discuss their relative efficiency, giving reasons for your answer *(Bombay B. Com. 1941)*
 8. What is functional organisation? What general principles must be observed in building up this type of organisation? *(Bombay B. Com. 1944)*
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CHAPTER XIV

INDUSTRIAL LABOUR

The rise of wage earning classes in India has been slow. The causes are not far to seek, before the advent of modern industrial era, by far the greater portion of people lived in villages where collective or individual ownership of land prevailed. The cultivator was economically independent. Whenever any extra labour was required, it was supplied by neighbors who were given a customary payment in kind. Industries were carried on small scale, cooperation among industrial groups was common. Industries in towns were carried on by master craftsmen who managed their affairs with the help of apprentices who in course of time themselves became master craftsmen and therefore there was no occasion for formation of wage-earning classes. With the rise of modern industrialism, there were three factors that helped the growth of wage earning class. Cultivation became unprofitable. Secondly artisans could not stand the competition of foreign machine manufactures, and they became wage earners to earn their livelihood. Thirdly the menials for whom the local needs had been outgrown and for whom the customary payment in kind was proving insufficient, began to move to the towns in search of employment.

Labourers as a class first appeared on farms as peasant farmers who hired themselves out for a part of time. It was not till the middle of last century that labour in organised industry first came into vogue chiefly in connection with the Public Works Department. A little later mines began to be developed and in the second half of the last century, establishments of plantations and factories attracted industrial workers from different parts of the country. Since the first world war, the pace of industrialisation quickened, and with it increased the number of industrial workers, and the extent of labour problems.

Characteristics of Indian Labour. The most important characteristic of Indian labour is its migratory character. The factory workers in India even to day do not constitute a distinct wage-earning class as in other countries. In India they are generally drawn from villages, and they retain their love for village life.

In spite of the dense population the fact remains that at times Indian factories feel shortage of hands, particularly of skilled ones. It can be partly attributed to the fact that villagers are drawn to the factories only when they can find no employment in villages, and when conditions in villages improve they leave the town; and the factories experience scarcity of hands.

The workers in India are drawn from distant places and areas. It is only seldom that in any industrial town its labour force comes only from suburbs. It means that in big towns like Calcutta and Bombay labour forms a hetero-

ganeous mass with various religions, different languages and customs. This accounts for lack of unity and organisation among the labour population of our country.

Another characteristic of Indian labour is its inefficiency, Indian factory worker is proverbially inefficient, and compares very unfavourably with the workers of other industrial countries. Attempts have been made to explain this inefficiency in terms of mathematical comparisons of output of the workers of India and other countries. This, however, is not the correct approach, as the Indian worker has to work under entirely different and decidedly inferior conditions than those obtaining in other countries.

Causes of Inefficiency. The causes of the inferiority of the Indian worker are many—some of them inherent and fundamental while others are ephemeral and transitory. Enervating Indian climate affects adversely the efficiency of the worker. Artificial humidification in cotton factories in India is highly injurious to the health of workers unless properly regulated. Industrial efficiency, on the other hand, depends upon different factors such as vigour and vitality, education and training, regular and steady attendance, good working conditions and efficient labour management, which in our country are grievously lacking.

The most important cause of inefficiency is the migratory character. The chief consequences of this incessant migration are a low standard of technical efficiency, an absence of responsibility arising from treatment of factory work as a disagreeable necessity. The workers from the villages come to towns for short periods usually to tide over temporary difficulties. As soon as they have earned a certain amount of money or conditions in the village improve they return, and leave the factories at the mercy of fresh recruits. Thus in many Indian factories production is carried on by workers fresh from the village. When the worker becomes fit for factory after several months' training he is thinking to go away. On the other hand it would be wrong to suppose that the Indian worker is himself an agriculturist or has any direct interest in it, though he contrives to regard his village as his real home. Nevertheless he is at heart a villager having a village tradition and a village upbringing, and very often the worker tries to maintain this contact. The contact may be close and constant, it may be elander and spasmodic or it may be only an inspiration rather than a reality.

The migratory character is explained by the fact that the worker has no attraction in the town. He comes because he is compelled to do so. As the Royal Commission on Labour remarked "he is pushed, not pulled, to the city." The growing pressure of population on land, uneconomic holdings, unemployment in villages, social disabilities escape from the money lender, avoidance of seasonal idleness—all these are causes which compel the worker to go to town in search of employment. Whatever be the cause, he retains his village connection and hopes to return at the earliest possible opportunity.

The causes of retention of the village connection are that as the worker is a member of a joint family, he always has some interest behind in the village. Moreover he leaves his family in the village as sufficient room is not available in the city or suitable employment for women is not readily possible. In the village women and children can find work and thus add to the family income. The worker does not feel quite at home in the artificial city life, and the strange environments subject him to severe strain and he becomes a victim to sickness and disease. The fatigued body and overstimulated mind find dangerous relief in alcohol and gambling.

The Royal Commission observed, that this connection has certain advantages and is a distinct asset, and the general aim should be not to undermine it, but to encourage and regularise it. The very tenacity with which many industrial workers with little encouragement have retained their village connections shows that the system has deep roots and cannot be abolished easily. There are certainly defects in the present system but these defects can be eliminated by the powerful and sustained efforts of the employers. Workers drawn from the villages have a better standard of physique than possessed by urban population, and the combination of rural and urban life brings a width of outlook which is apt to be lacking in purely urban or rural worker. Further in times of strikes, lockouts or unemployment the worker has always something to fall back upon. Moreover, there are important, educative effects, the healthy and wholesome influence of which cannot be overestimated.

Low wages. Vigour and vitality are lacking among the large sections of Indian population. Large numbers suffer from ill-health arising from malaria and other diseases which sap their vitality. The medical aid available at present is hopelessly inadequate. The worker due to his low wages and grinding poverty cannot procure the necessary aid for himself. Moreover a substantial portion of the wages is spent on drinking and on injurious drugs which give the worker a temporary relief from the fatigue of day's work. This leads the worker into the parlour of the money lender, and a part of wages goes either as interest or for return of the principal and therefore the worker is not able to obtain his necessities out of meagre wage that is left after such payments and consequently his efficiency suffers.

Lack of Education Facilities. General and technical education are lacking in our country and are responsible for irregularity of attendance so common in Indian Factories. The workers are mostly illiterate and lack of education stands in the way of promotion of workers to suitable and higher responsible positions, and the highest position he can at present attain is that of a jobber. Once he becomes a jobber, there is no initiative left in him since the industry offers no promise for further betterment, and consequently he degenerates into inefficiency.

Trying Conditions. Low wages, long working hours, trying working

conditions within the factory and unsuitable housing conditions without, spell disaster on the workers' efficiency. There is no suitable housing accommodation available inside the factory or even in the immediate neighbourhood and the workers often have to come from long distances. Lack of cheap transport system and long working hours during the day thus account for many late arrivals. The Indian worker is drawn from villages and he is not used to rigours of factory discipline. The absence of good working conditions, insufficient lighting, extreme temperatures, and long hours all breed in him a loitering habit, and in the end encourage absenteeism on the part of the worker, which is a sort of protective device to prevent them break down on account of enervating conditions in the factories. Absenteeism necessitates the maintenance of a 'reserve' force and leads to the employment of inferior substitutes and therefore to inferior work.

Defective Recruitment. The recruitment of workers is usually in the hands of a 'jobber' and every recruit has to pay his 'dasturi' to the jobber before he is taken. There is utter absence of any leave rules, there are arbitrary appointments and dismissals. Heavy fines without cause are inflicted, payment of wages is delayed, and consequently the worker loses interest in his work. The worker depends on the jobber for his appointment, transfer and promotion, and jobber therefore has to be continuously bribed. The jobber's income depends on the number of new appointments, and his interest lies in dismissals and new recruitments. Whenever men return from leave, they are refused to be taken and hence the high labour 'turn-over' in our country. Costs of production are increased, and efficiency of the worker suffers.

Cut off from his family and domestic surroundings, living in a dirty, highly congested hotel, working without break for long hours in a noisy, smoky atmosphere inside a dark, dirty and dingy factory, and not earning enough to make both ends meet in a decent manner, tyrannised by mahajans and jobbers for all sorts of dues, legitimate or not the Indian industrial labourer can hardly be blamed if he cannot take an active interest in his work and he is found inefficient in comparison with workers of other countries.

Inefficient Management: The organisation of labour in Indian factories is highly defective and leaves many things to be desired. Besides the faulty recruitment, there is no provision for training of the worker, there is no amiable direct touch between the employer and his men, and a sense of *esprit de corps* is generally lacking. There is no proper supervision of the work; usually the worker has to content with out-of-date machinery, defective plant, and inferior raw materials. There is no proper lay out of works; and co-ordination of various departments.

Housing of Industrial Population

A remarkable characteristic of the recent economic development in our country has been the growth of congested and crowded industrial towns. Though the progress of urbanization has been slow, yet the problem of housing

and congestion is perhaps more acute here than anywhere else and the country abounds in some of the worst slums of the world. Hardly in any industrial country, the growth of towns has been so colossal, the provision of labour settlement so inadequate and the state policy towards industrial welfare so callous as in our country. The appalling conditions of housing are largely responsible for the instability and consequent inefficiency of the Indian worker. The whole future of Indian industry is bound up with an improvement in the hygienic conditions in the great industrial centres.

The problem of industrial housing is easy where factories are set up in rural areas or at some distance, and where land is cheaply available. The labour is here housed either in neighbouring areas or in tenements constructed by the employer himself. In large towns however, like Bombay, Calcutta and Kanpur, the housing problem has been one of the most difficult. Land is scarce, and over-crowding is unimaginable. Insufficient accommodation, the dark and stuffy interior of the tenements and their squalid surroundings are the chief features of a working class colony. In practically every industrial centre the evil of overcrowding is present and there exists a shocking state of affairs. A very large number of houses for industrial population is the merest pretence of housing, incredibly damp, ill-ventilated and with no privacy and sanitation. Some of the huts are leafy shelters and others are so low that one could only crawl in and out of them.

In Bombay, the industrial workers are housed generally in one-room tenements called chawls. "The conditions here are most appalling. Personal inspection of one of these leaves recollections which will not be easily forgotten. Entering the shed and passing down a dark, narrow passage—so narrow that two persons could scarcely pass one another—one had to grope one's way to the doorway of rooms upon peering into these, it was impossible to ascertain whether they were occupied or not. Not a ray of light penetrated them, and this at noon on a bright sunny day. It was only on striking a match that the rooms were found to be inhabited,"

(Hurst)

"These chawls which differ considerably in appearance, construction and size, all have for their object the housing—one is almost tempted to use the expression 'warehousing'—of large numbers of the labouring classes in as cheap a manner as possible. The ground floor rooms are invariably dark, dismal and unhealthy, and often permeated with obnoxious effluvia." Many chawls are in a bad state of repair and a constant source of danger to the occupants. Subletting is common, and this aggravates over-crowding. Lavatory arrangements are hopelessly crude and inadequate.

In Kanpur conditions are almost similar. Workers are housed in single-room tenements called 'ahatas' and in order to meet the increasing demand for housing every inch of available space has been utilised to erect a new house. Rents are exorbitant. A house here is not worth its name, and may be called a den or literally a hut. Most of them are extremely insanitary

and over-crowded. The conditions are most appalling and about 64% of the labouring population is housed in these dark, dingy and disease-ridden hovels which neither protect the worker from cold blasts nor scorching winds. In rains water flows in tide and the hut is a pool and in summer it is essentially a fire-place. The Cawnpore Labour Enquiry Committee observed, "A night visit for a stranger to these areas is a risky undertaking—sprained ankle is a certainty while a broken neck by stumbling into a goodly-sized blind well is not an impossibility. No cleanliness, no conservancy, inadequate water supply, unfit roads and sanitation absent."

Conditions in other centres are not different, in some case, as Howrah they are worse. In Calcutta and Howrah the evil is more serious as about 80% of the labour of the province is housed in these two cities. Recently however attempts have been made to improve the conditions. Employers have built a number of suitable tenements in Calcutta, Bombay and Kanpur. It was in 1898 that Improvement Trust undertook the task. Though the trust has done really useful work, but it could not go very far, and lack of co-operation, nay, of presence of actually hostility between the trust and the municipal corporation, limitation of powers financial difficulties and opposition of landlords, compelled the Trust to confine itself to mere 'slum patching.' About 20% of the workers in Bombay, 15% in Ahmedabad, 12% in Sholapur reside in quarters provided by employers. The condition on the whole are extremely unsatisfactory.

In some industries conditions are, no doubt, much better. The housing arrangements at Jamshedpur by Tata, and at Nagpur by Empress Mills are commendable. In both cases employees are encouraged by loans given on liberal terms to build their own houses. Further slum clearance programmes have been undertaken by the municipalities in Calcutta, Bombay, Madras and Kanpur, and by Improvement Trusts and Ports Trusts. Considering the magnitude of the problem, whatever has been done is simply insignificant. A note in 1911 by Improvement Trust in Delhi showed that 88,000 persons lived in conditions of congestion prejudicial to health.

The Industrial Housing Scheme of the Government of India. The Government of India's new industrial housing scheme is by far the biggest plan of coostruction ever undertaken in India, and is also one of the biggest of its kind in the world.

Under this scheme, ten lakh houses for Indian workers will be constructed in the next ten years and finally they will be distributed as follows among the various industries: Factories seven and a quarter lakh; plantations a little less than two lakhs; and docks, etc., three fourths of a lakhs. This distribution is based on the number of workers under each category, who have not been provided with approved housing.

The total cost under this scheme is estimated at about Rs. 300 crores. The Central Government will contribute towards the capital cost to the extent

of two-thirds, in the form of an interest-free loan, while one-third of the capital cost is to be contributed by the Provincial Governments. It will be provided to build up a sinking fund out of which the loan will be repaid in 25 years. The annual recurring cost on this project, inclusive of liability under the sinking fund, repairs, etc., will come to Rs. 22 crores.

The execution of the plan will be the responsibility of the Provincial Governments subject to the supervision of the Central Government. For this, the Central Government will maintain a staff at their own cost. Employers' contribution will be in the form of rent for quarters allotted to their workers, and the rent so charged will not exceed 3 per cent. of the total cost. The workers will also pay in the shape of rent quarters occupied by them.

It is proposed to provide in the new houses, two rooms, a kitchen with space for storing food and fuel, and an independent bath-room, a lavatory, verandahs, both in front and at the back, and a courtyard in the case of single-storey houses. Electric light will be provided as far as possible. There will be provision for schools, shopping centres, parks and playgrounds, dispensaries, community radio receiving sets, libraries and reading rooms for the benefit of workers in each compact area.

This present scheme represents immediate and not the ultimate objective of our national Government. But it is a beginning in the right direction, and with the co-operation of the Provincial Governments and employers on whom rests a heavy responsibility, it will be possible to vouchsafe to the worker not only the comforts and amenities to which he is entitled, but also the human dignity, which has most unjustly been denied to him.

Effects of Bad Housing : 'Good houses mean the possibility of homelife happiness and health; bad houses spell squalor, drink, disease, immorality and crime and in the end demand hospitals, prisons and asylums in which we seek to hide away the human derelicts of society that are largely the results of our society's neglect.' Suitable living accommodation with cheap rents would remove many of the present evils. It is in these crowded areas that highest rate of infant mortality obtains. Over-crowding is the chief cause of many diseases like T. B. Housing has a direct effect on family life and therefore on labour turnover, domestic economy and vital statistics. Over-crowding has a direct effect on the health and efficiency of the workers, their growth is stunted, minds undeveloped and the bodies sapped of the vitality because of frequent illness.

If workers' efficiency is to be increased and in order to secure a contented labour force it is highly necessary that a vigorous housing scheme must be undertaken. Housing evils are a blot upon the society and a reflection upon the intelligence, right-mindedness and moral tone of the community. Some suggestions are made as follows :—

1. Decentralization of industries. Factories as far as possible should be scattered over wide areas, and there should be no concentration of them in few

towns. New factories should not be allowed to be set up in big towns. They should be rather encouraged to shift to rural areas where land is cheaper and easily available.

2. Strong municipal by-laws should regulate the house construction. In the cities so that new houses which conform to certain pattern, are allowed to be built.

3. Improvement Trust should be set up with sufficient powers to enforce its decisions, and municipal boards and Improvement Trusts should work in co-operation with each other.

4. Land Acquisition Act should be passed whereby the authorities be enabled to acquire land where available for house construction, and the available space in towns should not be allowed to be further congested by new construction.

5. In case of new factories responsibility for housing workers should be laid on the employers.

6. Co-operative schemes of house-building may be undertaken; cheap loans may be given to workmen together with other facilities for house construction.

7. There should be available cheap and efficient transport system whereby the workers can come to the factories and workshops easily residing outside the town at distances.

8. The government must assume the responsibility, and must take up housing programmes as one of the important subjects. Adequate grants should be given to Improvement Trusts, and they should be allotted some sources of recurring income.

Industrial Disputes

It is not known when the first strike of the entire labour force in an Indian factory occurred, but from the beginning there were loosely organised refusals to work. In 1877, workers of Empress Mills, Nagpur struck in a body because of a misunderstanding on wage rates. Since that time, frequent disagreements have arisen, many of which have been marked more by such ill-temper as is expressed in the throwing of a weaver's shuttle through a window than by considered demands.

The idea of common action came late to the workers as a whole. In 1890 one man wrote, "Workers are not yet organised, no record is kept of disputes, their occurrence being so rare and their duration never being more than a few hours." Another report says that whenever these slight strikes, as they may be called, take place, the invariable cause of them is on the part of employers fining the employees for bad work or attempting to reduce their wages. But such disputes are always amicably settled. About 1895 workers had developed a little consciousness, and these several strikes had taught them the power of united action. In 1905 electric light was introduced in the factories; working hours increased and many sporadic strikes took place.

Between 1907 and 1911, labour questions came to be discussed more and more. Upto 1908, however, workers' actions remained irregular and sporadic, when occasionally there was united action, it was rather of a mob aroused over a particular, temporary, purely local and often personal grievance, than that of a business like trade union.

During the war there was a certain amount of unrest and a number of sporadic strikes took place due apparently to changed conditions. The war swept all the old landmarks out of existence and created new forces and circumstances which compelled action radically different from the traditional policy of the past. Strike came to be regarded as an ordinary weapon of industrial warfare. Prices were high and wages relatively low and discontent was rising. All classes of population had been so stirred by the new currents set in motion by the war and the whole economic life so stimulated that after 1917 a large crop of strikes took place often over trivial and ill-defined issues. From 1919, the strikes were mainly directed towards an increase of wages and the securing of 10 hour day. Cases of concerted action, including large numbers of workers, became more frequent, sometimes more orderly and certainly more successful. No longer limited to single groups or departments within a factory. They came to affect group of mills, even all the mills of a given industry in big industrial centres. Employers were making large profits and strikes therefore were short-lived and often brought increased wages. The first strike affecting entire industry in cotton trade occurred at Bombay in 1918. By January 1919 practically all the 1,50,000 hands in all cotton mills were on strike. The strike situation was serious in 1919-21. The situation became rather quiet with the gradual restoration of normal conditions. The increased wages secured during this period continued but later when wage cut were made, they gave rise to fresh disputes. The years 1926 and 1927 were comparatively quiet.

The years 1928 witnessed industrial warfare on a scale not known before, and industrial unrest swept all over the country. The biggest strike occurred in cotton mills of Bombay affecting the entire industry, others being in Calcutta jute mills, Jamshedpur, Kanpur, Sholapur, and on East Indian and South Indian Railways. A court of enquiry was set up; relief measures were organised in Bombay. The Fawcett Committee considered the demands of workers fair and reasonable. In 1928 strikes, communist influence was responsible for violence and terrorism.

In 1929 the number of disputes considerably declined, the most important strike being in Bombay Cotton Mills. The provisions of the Trade Disputes Act, 1929 were utilised for the first time, and a court of Enquiry was set up. The Court of Enquiry laid the blame on the extremist section of the workers—*Girni Kamgar union*—an organisation influenced by communists.

In 1930 there was severe depression, and serious party conflicts arose among the workers so that their energies were directed towards their organi-

sation. Moreover the appointment of the Royal Commission on Labour raised hopes for reform. This meant a considerable decline in the number of disputes. Workers' organisation suffered a set back, and as depression deepened further cuts were made in wages which the worker could not resist. The number of strikes in 1932 was only 116—the smallest on record. The depression was at its worst in 1933, and workers were hit hard by wage reductions and mass unemployment. Workers organised strikes but failed. There was serious retrenchment over the railways. In 1934 there was a big strike in Bombay and Sholapur textile mills which in the end failed. This led to the passing of a Trades Disputes Conciliation Act by the Government of Bombay in 1934. Thus between 1930 and 1936 the number of strike remained fairly steady at 150 a year, year 1934 being an exception.

From 1937, however, judging from the number of strikes and that of the workers involved, unrest and discontent seem to have increased in intensity. The number of stoppages of work was 379 and 399 respectively in 1937 and 1938, affecting 64,600 and 40,000 workers and involving a loss in working days to the extent of 9 millions in each year. The advent of Provincial Autonomy and coming in of Congress Governments revived the hopes of the workers and the turn in industrial prosperity perhaps improved the prospects of successful strikes.

The effects of war on industrial relations are inconclusive. Judging from the number of stoppages of work it cannot be said that industry had a quieter period than before. The number of strikes since 1939 has been as high as in previous years. Indeed in 1942 was the high water-mark of disputes, the number of strikes being as high as 654. No other period could compare with this year in intensity and the dimensions of unrest. This was however an exceptional year and many of these strikes were due to political unrest. Since Government and employers were anxious to avoid any disturbances likely to hamper war production. With a view to reduce strikes and stoppages of work action was taken to promote various schemes of welfare work and negatively the government took powers, to prevent strikes and lockouts by making them a penal offence unless proper notice was given and until two months had elapsed after the Court of Inquiry or Board of Conciliation, if one was set up, had given their findings. Wages were increased and dearness allowances were readily sanctioned.

During the war period, the collective need of winning the war demanded temporary subordination of the profit motive of the capitalist and of the 'right of strike' from the worker. Immediately after the end of war, feeling that 'no strike pledge' is no longer in force Labour seems to have taken up a belligerent attitude. Consequently, some industries have been paralysed, while in others threatening proposals to down tools are looming large. Only recently the prolonged Tramway strike ended in Calcutta, there has been a

strike in the shipyard at Vizigapatam; workers in textile mills at Surat Navsari and Baroda have already gone on strike and notice of strike has already been given in various other industries. The retrenchment policy of Railways seems to have in store a serious upheaval.

The years 1945 and 1946 were the landmarks in the history of the industrial relations. The year 1946 was a peak year in regard to the number of strikes. The strike wave that swept India during the year 1946 was unique in its range. The strike fever afflicted almost all classes of workers from the scavenger to the school teacher. It attacked not only factories but also schools, banks, insurance companies, railways, municipalities, officers, tram and bus companies, police, navy and air forces. Dominating almost all spheres of economic activity, the strike wave was a challenge to the traditional ideals of industrial relations. It indicates that the old economic order is fast breaking down and the old processes and procedures have become ineffective and call for newer and fresher methods. In short, vast forces of fundamental nature are rising and our social organism heaves and tosses like a rudderless boat caught in a storm.

In spite of the incessant attempts of the Interim Government, all labour legislations, labour bills and conferences it is strange to see the growing discontent among labour.

Causes of Disputes. The published statistics relating to causes of disputes give a general idea regarding them. They are wages, hours of work, personnel, working arrangement, trade unionism and others.

Of the 4,622 disputes between 1921 and 1941, 2,644 or just over 57 per cent. were due to wages and bonus questions. This was inevitable because in India the wage is more or less the sole arbiter of the standard of living and has a greater significance to the worker than any other aspects of his conditions of work. The utter lack of any basis for fixation of wages in India, except the over-calculating bargaining power of the parties has provided a most fertile field for the growth of disputes.

In recent years the most important single cause of strikes was economic, the gap between low wage and rising cost of living which has showed an upward trend in all industries.

Questions concerning the relation between workers and management or between some workers and others compendiously termed as personnel rank only next in importance to wages. Alleged victimization, dismissal of workers actively associated with trade unions, non-recognition of unions, the dishonesty and corruption of jobbers and other intermediaries and reinstatement of certain dismissed persons—such matters are included in the 'Personnel' causes, and they account for one of every five disputes that occur. Such disputes are very common in India and in number they are without parallel in the world.

Hours of work are responsible only for a small percentage of the disputes

in our country. When the hours of work are excessively long, the workers try to resist them.

Working conditions such as insanitary conditions, bad housing, defective machinery account for a certain percentage, and there occur certain disputes for which there is no definite cause.

Recently trade unionism has been responsible for disputes and the willingness and refusal on the part of employers to recognize the trade unions has been a fruitful source of strikes. The trade union movement is gaining strength and has come to stay. The employers who are not accustomed in this country to labour organisation find in this new movement a challenge to their authority. Occasionally there is a temporary disturbance in relations, and minor issues are given prominence and lead to strikes.

There are certain causes which have no bearing whatever on economic problems or working conditions in the factories. Arrival at the industrial centre of a political leader, anniversary celebration of a great patriot, the declaration of boycott or a hartal are all utilised on occasions for a holiday, and have generally no more effect than loss of a working day unless an unwise employer takes disciplinary action. It at once gives rise to bitterness and may lead to strike.

Under the present system of recruitment, the jobbers often have great influence over men working under them, and if these are dismissed, the men sometimes out of sympathy but more through fear, strike work and refuse to return until the jobber is restored.

Absence of any definite code of rules concerning leave, holidays conditions of service, arbitrary dismissals without notice or change in the working conditions without their consent, fining the workers arbitrarily or subjecting their wages to unauthorised and illegal deductions very often embitter the workers, and they resort to strike and continue until their grievances are redressed.

There is no suitable and proper organisations or other machinery to carry to negotiations between men and employers. At times minor differences are given undue importance, which through a proper approach, could be easily settled. It has been found many a time that the workers don't know their own mind at the time of strike. Strikes are declared and it is only later that demands are formulated. If there are strong trade unions, irresponsible action will disappear. First the grievances and demands should be discussed among the workers, and then the demands be made known to the employer. It should be on the refusal of the employer to hear them or to redress their grievances that resort to strike should be taken.

Most of the Indian workers are illiterate and ignorant, and they still depend upon outsiders for leadership. Many unscrupulous persons have exploited this ignorance, and try to create disharmony and bitterness. "The 'briefless barristers' thrown up by an ill adjusted educational system, too often

have found an opportunity for notoriety and occasionally for social and political advancement "

The last but not the least is the cause that India is in a state of political ferment, and very often workers have been drawn into political controversies and any grievance is considered sufficient to down tools and carry on warfare with the employers.

Machinery for Industrial Peace : Any machinery designed to secure industrial peace can be evolved from two points of view—one to prevent the occurrence of strikes and lock-outs and to amicably settle the differences without open conflicts and second to settle disputes and bring about a conciliation when disputes have actually taken place. It is a trite saying that prevention is better than cure. Industrial warfare is a social phenomenon that has now become a permanent part of our modern existence. The distress, dislocation and danger caused by this war are so much that no body can afford to ignore them.

The causes of industrial disputes are economical and psychological and the lost thing would be to remove these causes. For this purpose two things are essential : (1) Welfare work in every individual factory which will provide for the formation of a 'Works Committee,' as also recommended by the Royal Commission on Labour where all questions affecting the worker's well-being will be examined and decided, and (2) the development of trade unions on sound lines, which will create in the workers a sense of responsibility. These committees would be the best for overcoming the psychological difficulties. These committees should consist of recognized representatives of workers and employers and should be entrusted with fairly a wide range of functions. The interest of the workers should be kept up by seeking their counsel and cooperation on all matters concerning them. The working conditions and rules should be decided in consultation with the workers because the fact that these conditions and rules are wisely conceived and fairly administered will conduce very much to harmony. It shall afford facilities for ventilation of worker's grievances and the differences than can be boiled down to irreducible minimum by discussions across a round table. On the other hand strong trade unions will prevent outbreak of sudden strikes without notice or without prior to seeking other avenues for amicable settlement. Further the payment of minimum wages in all trades where wages are low and of an economic wage where workers are organised and employed in organised industries will go a long way to reduce discontent.

The next step in evolving a conciliatory machinery is to supplement the works committees by Trade Boards at various centres which have been so successfully set up in England. India is a vast country and economic conditions differ from region to region, and province to province. To impose any uniform conditions throughout the country as distinguished from uniform principles would adversely affect the industrial development. They shall consist of

representatives of employers and workers in equal number, along with a few independent members of whom one would be the president. They will command the confidence of the parties and their decisions will be accepted as fair and just and therefore will not be likely to be easily challenged by either party. The system shall provide a way for settling wages on a fair basis, and will enable the settlement of fair wages and other conditions suited to different regions of the country. The board can set up a system of standardised wages agreeable to the workers throughout the region moreover this shall bring about a collaboration of employers and workers, and will help in bridging the present gulf that divides employers and workers and shall bring about better understanding and appreciation of each other's point of view and position. Local disputes in some of the establishment may be referred to the Board and may be amicably settled.

When disputes have taken place, machinery should be evolved to settle them. This would be done by setting up Arbitration Boards or Committees. How fruitful and serviceable both to employers and workers, arbitration can be, can be seen from the industrial history of Ahmedabad where a permanent Arbitration Board with Mahatma Gandhi as one of its members has been set up in the textile industry. For maintenance of peace it is essential that there should be a machinery to dispose of complaints, when they come, readily. All questions affecting the parties may be referred to the Board, and on disagreement may be decided by an impartial Umpire. The success of this provision stands as a clear achievement of Ahmedabad in face of other industrial centres of the country. Disputes have been less frequent, and so the stoppages of work, consequently to the interest of both employers and workers. There has been prosperity to the employers and higher wages to the workers.

State and Industrial Peace The injury done by the continued industrial warfare in modern times is too much to be ignored and the state has a part to play. The state can no longer afford to be silent or passive spectator or "look on itself to the holding of the ring while the disputants fight out their differences." This view cannot be regarded as satisfactory when we consider the great loss of money and material, the hardship to the community at large and the distress caused to the workers.

The primary thing that the Government should do is collection and publication of statistics having bearing over these matters, e.g., statistics relating to prices, wages, industrial production etc. This would help to bring about a ready adjustment in wages—the absence of which is the most important cause of trouble. Whether wages for an industry or for a class of work are adequate or not, or whether the demands for increased wages or wage reduction are fair or not are questions which depend for their right solution on proper statistics.

The government may also take to legislation, if necessary, in which provision may be made, at the desire of the parties to the conflict, for conciliation, mediation and arbitration,

As regards the first, the Government of India is now publishing certain index numbers relating to prices and wages. Several Provincial Governments also have undertaken the task, and though not entirely satisfactory, regular data are available on the problem.

In India, up to 1929 there was no statutory provision for constituting any machinery for the prevention and settlement of labour disputes. For the first time in 1929, the Trade Disputes Act was passed. It empowered the Government to refer labour disputes to a Board of Conciliation or a Court of Inquiry. The power vested in the Government was not quite freely used and in a few cases only industrial disputes were referred either to a Board of Conciliation or a Court of Inquiry. The conclusions and the recommendations of the Boards or the Courts could not be enforced and made binding on the parties, as there was no provision in that behalf. In public utility services, fourteen days' notice before a strike or lockout, was made compulsory and a strike or a lockout without notice in such services was illegal and punishable. While the right to strike, the only effective weapon that the workers possess, was restricted, neither any standing Conciliation machinery was provided for nor was it obligatory on Government to refer industrial disputes to a Board of Conciliation or Court of Inquiry. To this extent, therefore, the Act was halting and one-sided.

In 1938, the Trade Disputes Act was amended. The Government was empowered to appoint Conciliation Officers charged with the duty of mediating in or promoting the settlement of trade disputes. The power to establish a standing Conciliation machinery, however, remained to a large extent in the statute book. However, in the Province of Bombay, the Government established a permanent Conciliation machinery under the Bombay Trade Disputes Conciliation Act, 1934, and the Bombay Industrial Disputes Act, 1938, which is recently replaced by a more comprehensive measure, viz., the Bombay Industrial Relations Act, 1946.

During the War, it was usual to resort to compulsory adjudications of industrial disputes. By Rule 81A of the Defence of India Rules, the Central Government was empowered to make rules for prohibiting strikes and lockouts in connection with any trade dispute, for referring any dispute for conciliation or adjudication and for enforcing their decision. This power was more freely used both by the Central and the Provincial Governments than that under the Trade Disputes Act, 1929.

In the light of the experience of the working of the Trade Disputes Act, 1929 and that of Rule 81 A of the D. I. R., the machinery for prevention and settlement of industrial disputes has now been thoroughly overhauled and incorporated in the new Industrial Relations Act, 1947. The Act provides for the compulsory establishments of Works Committees in industrial establishments employing 100 or more workmen. The duty of Works Committees will be to promote measures for securing and preserving amity and good relations between employers and workmen and to that end to comment upon matters of their

common interest or concern and to endeavour to compose material difference of opinion in respect of such matters. This is one of the special features of the new Act and will go a long way in helping the workers to carry on negotiations and secure collective bargaining. The Act provides for compulsory conciliation by officers of the Conciliation machinery to be set up by Government in disputes relating to public utility services. Conciliation in other disputes is also provided for. Conciliation proceedings must be completed within the prescribed period. In case conciliation proceedings fail, the Government has been empowered to refer the dispute to a Board of Conciliation for promoting a settlement thereof or to an Industrial Tribunal for adjudication.

The Conciliation machinery can work as soon as a dispute is apprehended or threatened as well as after a strike or lockout is started. It is the function of a conciliator to see that the deadlock ends as early as possible and normal and peaceful working of the establishment is restarted.

The guiding principles of legislation should be that voluntary conciliation machinery is allowed to develop to the fullest extent, and the right of sudden strike in public utilities and industries of national importance should be restricted by law so as to ensure protection against sudden stoppages of work which may endanger the community's wellbeing.

Trade Unions

The individual workman is almost always at a disadvantage in bargaining with his employer. The employer has not only better bargaining power but in the act of bargaining his education and training place him in a superior position as compared with a single worker. With a view to protect the interest of the workers trade unionism has evolved which replaces individual worker by collective bargaining.

Trade Union is a 'continuous association of wage earners for the purpose of maintaining or improving the conditions of their employment.' True trade unions have two-fold objects to maintain and consolidate what has been attained, and to attempt for further improvement in conditions of workers. The idea of a trade union is ordinarily associated with strikes and lockouts, and therefore by some it is mainly considered to be a fighting body always ready for industrial warfare. But as is clear from its definition, and as can be seen from its constitution strikes are only the means and not the end, which have to be resorted to when other attempts fail, to improve the lot of the worker. Today a trade union is given the foremost place as the agency which can promote peace, bring about a better relationship between employers and workers, and which can bring about many-sided improvement in the worker's living conditions.

Its main objects and functions are (a) to promote friendly feeling and to foster a spirit of brotherhood and cooperation among the workers, and to organise them, (b) to consider the question of their various disabilities with regard to their work and wages and to try to bring about their removal by all lawful means, (c) to promote friendly and harmonious relations between workers and their

authorities ; (d) to maintain funds for the relief of members in sickness and distress ; (e) to undertake benefit schemes such as sickness insurance, provident fund, cooperative credit, medical relief etc ; (f) to declare, organise and conduct strikes, to carry on negotiations with the employers, and to settle disputes amicably ; (g) to provide legal aid in need ; and (h) to take such other steps as may be necessary to ameliorate the social, educational and economic conditions of the workers and their dependents.

It is clear from the above that the primary aim of a union is the social and economic uplift of its members and all its activities are directed to achieve that end. It may undertake such activities as propaganda work to enlighten public opinion and to win their sympathy and support ; collect statistics in order to form a correct idea of the condition of the workers ; protection of rights of unions ; the study of labour questions ; the coordination of efforts of different unions and the promotion of the moral status of the worker by temperance and other similar movements.

Other important service rendered by trade unions is that they have a great educative influence on the workers, train them in organisation and discipline and pave the way for government legislation.

Trade Union Act, 1926. The Act gives a legal recognition to the trade unions, and defines their legal position in precise terms. Registration of the union is optional under the Act, but certain obligations and privileges are conferred on registered bodies, not available to the unregistered. Registered unions must have a name and must define the objects for which they are constituted. They must furnish audited accounts and at least one-half of the members must be actual workers. As regards privileges, the Act grants immunity from criminal liability to all trade union officials acting in furtherance of the legitimate objects of the union. Nor are they liable to be indicted for conspiracy. The law further provides that (a) no suit shall be maintainable at law in any civil court against any officer or member of a registered union for any act done in furtherance of the legitimate objects of the union, on the ground that such an act induces some other persons to break some contract of employment ; (b) that no suit shall be maintainable in any civil court against a registered trade union for any act done by any person acting on behalf of the union, provided such acts are not authorised by the union ; and (c) that a registered union may collect funds from its members on a purely voluntary basis for the promotion of any civil or political interests of its members.

The Trade Union Amendment Act of 1916 provides for compulsory recognition of trade unions by employers in certain circumstances. It also specifies certain acts as unfair practices on the part of recognised trade unions and certain other acts as unfair practices on the part of employers. It also provides that a trade union shall not be entitled to recognition unless it is a representative trade union ; its rules do not provide for the exclusion of members on communal or religious grounds and lay down the procedure for declaring strike.

History. In India the association of labourers for promoting common labour interest is of recent origin. The first record case of collective representation took place in 1881 when a conference of the workers was called for the purpose of drawing a memorial to the factory commission. But the idea of a common action came late to the workers as a whole. The first important step towards organising labour was taken by one Mr. Lokhanday in 1890. A union known as Bombay Mill Hands' Association was organised to present a memorial to the Government in connection with the amendment of the Factory Act. This was a loose combination rather than a corporate body. It had neither a definite constitution nor a definite paying membership. In 1897 the Amalgamated Society of Railwaymen of India and Burma was formed, and it exists to the present day. Its functions were however more fraternal than militant. Other unions started in the beginning of the present century were the Seamen's Union, Calcutta, and Postal Union, Bombay. In 1907-8 when Morrison Committee was making its inquiry, a few unions were discovered in Bengal. There was one Mohammedan Association and the other Indian Labour Union. The latter in spite of its ambitious name appears only once in a footnote to the Committee's report and Mohammedan Association could hardly be called a trade union. In 1910, a worker's welfare organisation known as Kamgar Hitwardhik Sabha was formed, and continued upto 1922 but was never very active.

It was not until 1915 that trade union movement really began in India. It was only during the early post war years when the grave economic difficulties of labour following the phenomenal rising prices and the general political tension together with the world-wide uprising of labour consciousness, instilled into the minds of the labourers the necessity for combination for advancing their own interest. "With the social mind surcharged with war spirit, political agitation and the revolutionary ideal, the labouring classes could no longer remain patient and tolerant under the old social wrongs and the new economic disabilities. There was a rapid development of trade unions in this period. The first union was formed at Madras, and it was followed by similar organisations at other places. Thus the years since the first world war were a time of unrest and agitation with much experimentation in trade unionism. Especially in earlier years many unions were mere strike committees, came into being to die within a few hours when or before the immediate contest was won or lost. They were generally isolated from one another without any solidarity among them. It was at this time that need for coordination was felt unexpectedly. Delegates from some central and representative organisation of labour were to be sent to the International Labour Conference, and hence the stimulus to coordination. The local unions were federalised, and then provincial federations were formed. The first All India Trade Union Congress a national federation of all unions--was held in 1920. In 1922 Central Labour Board was formed and in the same year was formed the All India Railwaymen's Federation followed by Postal and

Telegraph Union. The main difficulty during this period was that leaders were not available from within the labour ranks, and therefore the unions were thrown into the waiting hands of outside agitators.

Employers refused to recognize these unions. Workers were victimized, recognition was refused, and Criminal Procedure Code was amended and trade union activities were made illegal. In 1920 in the Buckingham Mill case an injunction order against the Madras Union was given and labour leaders found that they could be prosecuted for bona fide union activities. N. M. Joshi tried to influence government in order to secure protection for the workers but his labours bore fruit only after 5 years, and in 1926 Trade Union Act was passed. This led to rapid increase in the number of Unions.

The height of the movement was reached in 1928-29 when Communist influence came to be felt, and they captured most of the unions. The most important union under their influence was Girni Kamgar Union with more than 50,000 members. Their other unions also showed a marked increase in membership. They organised a general strike in Bombay in 1928 and achieved a success. But the activities of the communist members led to troubles and rioting in the city, and a number of important leaders were arrested, and prosecuted. In 1929 they again organised another general strike which continued for pretty long time. A Court of Enquiry was set up, and its findings went against the Kamgar Union on which rested the sole responsibility, according to the Court of Enquiry for the strike. This unfavourable report against one of the most important organisations of workers much discredited the trade unions, and the movement got a serious set back.

In 1929 in the 10th session of the All India Trade Union Congress, the Communists captured the executive of the Congress and then resolved to indulge in extremist activities e. g. to affiliate the Communist International. At this moderates under N. M. Joshi seceded from the Congress and formed the Indian Trade Union Federation. Railwaymen's Federation also severed its connections from that body. In 1931 a further split took place when the Extremists formed their own All India Red Trade Union Congress. After 1931 delegates to the International Labour Conference were sent from the Indian Trade Union Federation. The several splits among workers' organisations greatly undermined the movement and efforts were made to bring about a unity. In 1931, a Trade Union Committee was formed which found that the gulf between the Communists and others was too wide. In 1933 National Trade Union Federation was formed including all organisations other than Communists. In 1935 the two sections of the Congress were combined. It was however in 1938 that grounds were prepared for final unity, and a provisional agreement was signed which was ratified in 1940.

This solidarity unfortunately, could not be maintained for long. There came the break up in 1940. On the question of war effort the Trade Union Congress passed a resolution of neutrality. This attitude of indifference was

not approved by Dr. Asf Ali, President of Seamen's Union, and his union therefore seceded. Another organisation was formed by Mr M. N. Roy under the presidentship of Jamna Das Mehta. This organisation stood for an all out support to the war effort. At present, the Indian National Trade Union Congress is recognised to be the most representative trade union organisation in the country. Affiliated to it today are 800 trade unions representing 12 lakhs of workers. Next to it comes the All India Trade Union Congress. Time was when the All India Trade Union Congress was the representative of workers but with the infiltration of Communists its membership, after the I. N. T. U. C. had broken away from it, was steadily dwindling. Besides the A.—I. T. U. C., there is the Hind Mazdoor Sabha run by the Socialist party and in the first week of May 1949, the United Trades Union Congress has been formed of which Mr. K. T. Shah is the President and Mr. M. K. Bose the General Secretary.

Achievements of Trade Unions in India. The trade union movement has recently made a remarkable progress in India. The movement is fairly wide spread and has taken deep roots. They are no longer mere strike committees, they are now better organised, maintain office, and are permanent organisations with considerable following. Advent of Provincial Autonomy has given an incentive to the movement, as trade unions now send representatives to Provincial Legislatures. At the end of 1941, there were 750 unions with a membership of 6,50,000. These unions wield influence which cannot be considered negligible.

The history of the movement is short, and hence it would be difficult to assess the work or achievements of trade unions in India. It may be however, safely claimed that they have a fairly large number of successes to their credit, and have been able to help themselves considerably. In the early years of their formation they were able to secure considerable increase in their wages, brought about a reduction in working hours, and in 1926 were successful in preventing wagecuts. Another important to the credit of trade unions in India is that they have brought about a change in the employer's attitude towards labour. In place of indifference and hostility, they have now a feeling of sympathetic concern. The Railwaymen's Federation intervened successfully in 1925 in B. N. R. strike, and in 1927 in Kharagpur workshop lockout.

In spite of the recent progress, it must be regretfully admitted that even today organised association of workers in our country is far below the stage of development which it has reached in other countries. Hardly 5 per cent. of our industrial labour have yet joined the unions. Unfortunately most of our unions are only hollow structures and have been kept alive through the zeal of outsiders, with insufficient funds and fictitious members. Few Unions pay unemployment, sickness and old age benefits. Their fraternal or 'mutual help' side is practically undeveloped and they have confined themselves merely to militant activities. There is however an exception and that is Textile Labour

Association of Ahmedabad. It provides a host of welfare schemes in the form of hospitals, education, cheap grain facilities for co-operative credit and amusement and recreation of the workers. It publishes a weekly paper, and members get more than the value of their money paid as subscriptions.

The future is however bright. It is possible that with the spread of literacy, Indian industries will attract a type of more enlightened workmen, who shall provide from among themselves good labour leaders. A healthier and solid structure may then be raised. A great responsibility rests upon the labour leaders. In the hands of Extremists, the future is very uncertain and unpromising. Many of the present unions are handicapped by internal weakness and external opposition, which is accentuated by an unreal membership, inadequate finance, indifferent leadership, unbusinesslike methods. It is expected that in years to come the movement shall gather momentum and India would be proud of as good organisations of labourers as other countries of the west.

Difficulties of Trade Unions in India. The causes of the slow progress of the trade union movement in India are the many difficulties that the movement at present faces, the most important of which are as follows :—

1. Except on railways, workers are mostly illiterate or without sufficient general education. They are not amenable to discipline, and are unable to guide the union with prudence and tact.

2. Indian labour is generally migratory and of heterogeneous character. They are drawn from distant and strange places with their different languages, social customs, habits and traditions. Most of the workers are frequently leaving an industrial centre or are frequently changing their employers, and therefore they are less inclined to maintain a constant interest in any organisation.

3. Many of the workers are absolutely illiterate, ignorant and lack democratic spirit. It is difficult to inculcate the principle of unionism in them. As a result the workers are reluctant to pay their subscriptions and it is difficult except when dispute is imminent to convince the worker that payment of subscription is worth while.

4. Workers in India are generally low-paid and over worked and those whose wages and leisure are just sufficient to keep them working can hardly think of any association whatever. The wages are insufficient, and most of the workers cannot pay any subscription. If they can pay at all, the subscriptions are very low which do not provide adequate finance to the unions, and hence they cannot be as useful as they are expected. Further the worker hesitates to pay subscription for purely problematic advantages and considers his subscriptions as insurance against all dangers or expects in return an increase in his wages and that too within a reasonable period.

5. Difficulty of collecting subscriptions is also important. At times money collected is embezzled and/or does not reach the treasurer readily. Employer

discourage the collection of subscriptions in the mills where it is only possible to realise it.

6. The hostility of employers and jobbers has been another stumbling block. It is only too true that workers showing any sympathy for unionism are victimized, intimidated and dismissed. There are grave difficulties of recognition and very often employers place restrictions on the composition of the executive of the unions and their leaders, which if satisfied, leave a union only in name and then the union cannot achieve anything substantial. At times against genuine organisations of workers, bogus counter-organisations are set up by employers and these are readily recognized and actively subsidised to counteract the influence of real organisations. Other unscrupulous means such as recruitment of back-door labour corrupting and bribing the leaders and union representatives are adopted to weaken a union, to break its power and to smash a strike.

7. Another great difficulty of sound and solid trade unionism in our country is that workers are scattered over a vast area, and in some cases workers are simply inaccessible, e.g., in Assam plantations. Information regarding them is suppressed and outsiders are prevented from coming in touch with them.

8. One of the greatest handicap has been the lack of good leaders. It is still too dependent on outside leadership. This is a very great source of weakness. Many of these outside leaders are lawyers and other professional persons. They lack the technical knowledge of the industries, as well as the complete sympathy with labour that comes as a result of "having gone through the mill." Some leaders are connected with several unions at the same time and are therefore unable to give enough attention to any one of them. Very often the "briefcase barristers" thrown up by an ill-adjusted educational system have here found an opportunity for notoriety, and occasionally for social and political advancement. It has been truly remarked that workers' contributions were embezzled. Some of the leaders were sincere, while others were merely propagandists and mischief mongers who have exploited the ignorance of the workers for their own personal advantage. The Royal Commission observed that true vigour can come only from within and that Indian unions needed to become self-reliant and to develop an internal collective will by the training of their workers and the closer association of the members of the union. It was also recommended that unions should widen their range of activities.

Wage Payment

The object of every scientific manager is to keep the labour costs to the minimum, and this in other words means that amount of wages and method of their payment will be so adjusted as will be conducive to the maximum of production at the minimum of cost together with a contented labour force. Thus the problem of wages has two important aspects. It has a *social* aspect from the point of the workers' physical and moral welfare, and an *economic* aspect from the point of view of industrial costs. Low wages are, in fact, a

monaco to the health and welfare of the community and have serious economic consequences. They constitute small purchasing power and slight economic demand. Moreover, low standards of living are the cause, as well as the result, of industrial inefficiency. If wages are adequate and method of wage payment satisfactory, considerable progress is made towards amicable industrial relations and encouragement of efficient production. In the absence of a satisfactory wage system, no amount of benevolent paternalism functioning through an array of welfare activities will suffice to make employees contented and efficient.

Understanding this significant fact, the major requirements of a satisfactory wage system, generally recognised by authorities may now be discussed as follows :—

The first and foremost criterion of a satisfactory wage system is that it should be of benefit to both employers and employees ; that is, it should decrease costs and at the same time permit the ambitious worker to raise his earnings above the prevailing base rate. In other words, a satisfactory wage system should be determined with reference to the productivity of labour and the capacity of industry to pay. An increase in productivity of labour, other things remaining the same, lowers unit costs and thus becomes really the ultimate basis for increases in real wages. Similarly, no industry can increase wage rates beyond what its financial condition permits. The dangers and difficulties of inflicting on industries a wage beyond "what the trade can bear" at any given point of time are many.

Secondly, it should guarantee a minimum wage which may provide for the full satisfaction of the bio-social needs of the workers. There is a growing feeling that industry was made for men and not men for industry, and that industry can and should provide the workers with decent conditions of life. This fact has long been recognized, but Henry Ford was one of the first to make a practical experiment along these lines. One of the most interesting manifestations of this belief is modern legislation in behalf of a "living wage" or "minimum wage".

Thirdly, a satisfactory wage system should provide a proper incentive to the workers. It should encourage a worker to exert his best. The incentive reward should be directly connected with the worker's efforts and not be distant and dependent upon general conditions or the work of his fellows. A worker should be paid according to his individual character, energy, skill and reliability and not according to his position he fills. In the setting up of a wage system both quality and quantity of work should be considered. The principle of bonus reward should be liberally applied. Bonuses should be devised for both quantity and quality of work, for waste elimination, for length of service, for prompt attendance at work and for accident reduction in order to stimulate production and efficiency.

Fourthly, the basis of a good wage system must be set, if possible, so as to be permanent and consistent. Nothing so quickly leads workmen to distrust

such a system as changes in basic rates and principles. This means that before such a system is introduced a careful time study, motion study and standardisation should be resorted to. Rates based on mere guesses or estimates are not likely to be long successful.

Fifthly, the system should be simple and comprehensive. It should be easy to apply and easily understood by the worker so that he can calculate accurately his increased earnings. Complicated systems which the worker cannot readily understand are of doubtful value. Moreover, the system should be such as will be easily handled in the office and will result in shortening of the records.

Sixthly, the system should be such as would result in securing industrial peace. It should promote happy, healthy and cordial relations between employer and the employed. It should knit together the conflicting interests of labour and capital and should replace strife and industrial war by a sense of mutual regard and co-operation and a spirit of compromise.

Finally, it should aim at increasing participation of labour in management. It is a well-known fact that unless and until the workers are given increasing facilities for sharing in control and management of an undertaking, they will never take personal interest in its affairs. But by the introduction of such a measure, a new sense of ownership and responsibility may be infused into the minds of workers, and this may ultimately result in efficient production, elimination of waste of labour and raw material and reduction of costs of supervision and control.

The various systems of wage payment that are in vogue in modern industrial establishments are given below.

(1) **Time or Day Wage.** It is the system where the worker is paid in strict accordance with the time spent on the employer's work at so much per hour, per day, per week, per month or per year. Advantages and drawbacks of this method are as follows:—

Advantages. This method of wage payment is applicable where others may fail on account of the difficulty of measurement of output, and in such case this method is indispensable.

As the worker is not in hurry, work is not degraded by reason of speed of performance and he can bring to bear on his work his ideals of craftsmanship resulting in the performance of carefully finished goods.

A standard wage is favoured by workers, and a sense of solidarity is developed within the wage group.

Calculations are simple and easily intelligible to the workers, and therefore very attractive to the workers in India who are largely ignorant and illiterate.

Drawbacks. It gives little or no recognition to the fact of differences in the worth of men. Though in some cases superior workers may be given harder work with higher wages, still in general no adjustment is accurately possible.

There is no incentive to harder work. The worker knows that as long as he can manage to do the least work without exciting comment or affecting his dismissal, he need not do more, because harder work does not bring him greater reward.

A large amount of strict supervision is required in order to get sufficient work from the worker. It increases over-head costs. "The inherent and most serious defect of even the best managed day work lies in the fact that there is nothing about the system that is self-sustaining. When once the men are working on a rapid pace, there is nothing but the constant, unremitting watchfulness and energy of the management to keep them there."

The specially skilled, ambitious and well-trained worker is given little or no inducement to utilise his talents to the best advantage of the firm employing him. F.W. Taylor criticised the method thus: "The men are paid according to position which they fill and not according to their individual character, energy, skill and reliability. The effect of this system is distinctly demoralizing and demotivating; even the ambitious men soon conclude that since there is no profit to them in working hard, the best thing for them is to work as little as they can and still keep their position. And under these conditions the invariable tendency is to drag them all even below the level of the medium."

(2) **Piece Wage System.** It is a system of payment by results. Under this method, the rate of payment is correlated to the quantity of work done, i. e., each worker is remunerated at so much per certain amount of work finished, irrespective of the time taken.

Advantages. It is a more equitable method as it takes into account the varying efficiency of the worker. The comparative ability of the worker can be readily estimated by the amount of work performed and each man is rewarded according to merit and output.

The work man is encouraged to exert his best energies, because his wage-bill depends entirely upon the quantity of work that he can turn out. It thus leads to larger output, and makes supervision unnecessary, and cost of attendance minimum.

3. Over-head costs are reduced, and manufacturer is benefited; wage-bill is increased and the worker is benefited; and the price is lowered and the consumer is benefited.

Drawbacks. The great difficulty with the administration of this method is the tendency to disagreement between the management and the employees as to the equity of the rate to be paid.

There is the natural inclination on the part of the workmen to earn as high an amount of wages as possible and an equal desire on the part of management to obtain as low a cost per unit of production as possible. In the former, workers try to turn out as large quantity of work as possible, and therefore the work is rushed through and the quality suffers. In the latter, when the management thinks that workers are earning too much, there is the danger

that the rates shall be nibbled with.

The workers under the inducement to earn high wages may over-exert themselves, exhaust their energy and secure a minor advantage at the sacrifice of much greater future loss. In 'sweated' industries where the rates are low and where a living wage cannot be earned except by working at high pressure, the worker is impelled to over-work and consequently to over-strain himself.

The method is inapplicable to certain kinds of work, especially work of responsible nature. Generally speaking, it is inapplicable at the two extremes of labour, the most highly skilled and the least skilled, for instance the business entrepreneur and the general labourer.

(3) **Progressive Wage or Premium Bonus System** Scientific management experts considered the above two methods of wage payment and found them wanting. They criticised these methods, and attempts were made to evolve new methods of wage payment which would do away with the above defects. These new methods are technically called 'Progressive Wage' system or Premium Bonus methods. They are based on the combination of time wage and piece wage methods, and the worker is paid, besides a guaranteed minimum, in addition something, called the bonus or premium, if his work exceeds a certain standard laid down. The advantages claimed for these methods are :—

To stimulate production by encouraging workers to earn more than the average wages

To obviate the tendency of cutting down the rates by combining the workman's bonus with some benefit in the savings of wages to the employer.

To help towards economical production by reducing the wage and production cost per unit.

To unify the conflicting interests of the employers and the employed so as to promote and sustain increased efficiency and smooth working

There is a number of variations of these methods, the chief difference between them lying in the way in which the bonus or premium payable to the worker is calculated. The chief of them may be noted below :

(a) **Hesley System.** Under this system, a standard output is laid down, and every workman who produces this output within the time specified, is given, in addition to his normal day wage, a portion of the wages for the time saved. Thus supposing that the standard time fixed for a work is 10 hours and the worker finishes it in 6 hours, the worker shall receive his normal time wage, i.e. wage for 6 hours at the usual rate and in addition he shall be paid a certain fixed percentage, say 50%, of the time actually saved. Thus in all the worker shall be paid a certain fixed wages plus 50% of the time saved by way of bonus, i. e., further 2 hours' wages.

(b) **Rowan System.** Under this method, the worker gets his wages for the time worked at the usual rates. Thereafter the worker is given by way of bonus, if he completes the work within the fixed time, a certain amount on the basis of time saved. The bonus is actually the proportion of the time actually taken to perform the job, which the time saved bears to the standard time allowed to do the job. Thus if a workman is given a work to be completed in 10 hours at the rate of Re. 1/- per hour and if the job is finished in 8 hours, his remuneration under this method will be calculated as follows :—

Time taken 8 hours for which wages are Rs. 8

Time saved—2 hours = 20% of time allowed

∴ The bonus would be 20% of time taken = $\frac{1/2/7}{9/2/7}$

The Rowan System is less favourable to the workmen while compared with the Hasley System, as it is possible under the Hasley System, to earn a higher wage, because in this system the worker receives a fixed percentage of increasing sum, whereas in the case of Rowan System the bonus is decreasing proportion of decreasing sum. It shall be interesting, however, to note that where the time saved is not much, Rowan System would be more favourable to the worker.

(c) **Differential System or the Taylor System.** Under this system, if the worker performs the standard work within the standard time he is paid the standard wage plus something, while one who fails to do it, he not only gets less for less work, but is also paid at a lower rate.

(d) **Collective Wage System.** The various methods discussed above are applicable to individual workman. The adaptation of the above methods is made whereby a group of workmen is required to work on the application above methods instead of individuals. There are a number of adaptations, such as (1) Collective task wage, (2) Collective piece wage, and (3) Collective progressive wage, the chief of which is the Output Bonus System or Priestman System. Under this system the standard weekly output is agreed upon between the management and the workers based upon either a number of persons or hours per week. On the number of workers or working hours being increased or reduced, the standard output would necessarily be adjusted accordingly. At the end of each week, the total output is measured in definite units, and in case of an increase over the standard output, a bonus becomes payable to every employee at the percentage the increased output bears to the agreed standard.

It need hardly be pointed out that in addition to the above, there are several Bonus or Premium methods which are modifications of one or the other of the above methods and which may differ only in detail devised to meet particular conditions. The sole objectives of all these methods is quickening of production, and in brief they constitute a combination of the normal day wage and piece wage.

is difficult simultaneously to pool separate rights and to protect them against each other.

The reward is not available immediately after the effort. The profit is payable only once a year and is dependant upon the results of annual accounts. The uncertainty of the benefit and remoteness of the reward tend to dampen the enthusiasm of the worker.

It is well that when there are profits, they are shared both by management and workers. If, however, there are losses, the workers cannot be supposed to have a share in them. They are borne entirely by proprietors. It is an arrangement where loss falls only on one section while profits are divided by two parties.

Most businesses have their ups and downs. What may be very nice for all parties in prosperous years may become a source of embarrassment in bad years. "Employers are likely to strike a bad year, and when this happens, profit sharing is a serious embarrassment. It is very difficult for the trader to explain to his workers that he has made no profits. There are occasions when such statements may have harmful effect on credit and be even dangerous. Instances have occurred where employers, rather than make such admission, have paid away 'profits' which had no real existence."

In a large business employing a large number of workers, the share of the profit to each worker cannot be large, and the workers do not take any great interest where the reward is slight and small, and even which may disappear sometimes.

Profit sharing schemes in order to be successful needs a religious spirit behind it, i.e., they should proceed from unselfish motives. The idea of a charitable institution or warm-hearted philanthropy on the part of employers is resented by the workers while for the employers, human as they are, it becomes difficult to be self-less or to take different attitude.

The other great drawback is that accounts can be juggled and manipulated to the detriment of the workers. They might have worked very hard, yet at the end of the year they may find to their disappointment that there have been no profits in the business. Workers are not directly responsible for the amount of profits. Though their contribution is valuable and indispensable, yet it is of secondary importance. "Though an employee may exert himself to the utmost, there may be loss in place of profits owing to trade depression, inefficient and wasteful methods of buying and selling, defective arrangement in internal administration."

In view of the drawbacks and difficulties mentioned above, the profit-sharing schemes have failed in many a concern, though in some businesses, where the scheme was well-conceived and properly applied, they have been extremely successful to the mutual advantage of employers and employees.

5. Co. partnership Co-partnership, as distinguished from profit-sharing, has two elements in it, the first of profit sharing and the second of control

sharing, a part of the capital of the concern being owned by the workers. The chief features of co-partnership are :

(a) That the worker shall receive in addition to the standard wage some share in the final profits of the business :

(b) That the worker shall accumulate his share of profits or part thereof in the capital of the business .

(c) That he shall acquire some control in the business in two ways : (1) by acquiring share capital and becoming a shareholder, and (2) by formation of co-partnership committee, having a share in the internal management.

Advantages Almost all the advantages pertaining to profit sharing are also claimed for co-partnership. Besides them, the following advantages may be mentioned :—

There is wide diffusion of ownership, thereby promoting 'industrial democracy' ; it also gives to the workers a real sense of ownership, a personal interest and feeling of responsibility for the success of the undertaking.

Wastes of labour turnover are reduced, and workers are encouraged to save. Thus thrift and investment are developed.

Workers are co-proprietors, and therefore closeness between labour and capital is increased. Workers have a share in the control and management, and may sometimes bring sufficient pressure to increase their own wages.

The worker plays a triple role, he shares wages as employee, gets dividend as part owner of capital, and has a directing voice as a shareholder.

Drawback. Besides the many drawbacks of those mentioned in profit-sharing that are applicable also to co-partnership, the chief other defect is that it is applicable only to joint stock companies, and not to proprietary concerns.

The Proposed Profit-sharing Scheme. The question of allowing workers to have a share in the profits of the industry was brought to the fore in December 1947 by the Industrial Dispute resolution adopted at the Industries conference. The Resolution stated that capital and labour will share the product of their common effort after making provision for payment of fair wages to labour a fair return on capital employed in the industry and reasonable reserves for the maintenance and expansion of the undertakings. Later on, the Government of India, in their statement of industrial policy made it clear beyond a shadow of doubt that labour's share of the profits should be on a sliding scale normally varying with production. Subsequently, the Government of India appointed an Expert Committee on profit sharing on the 25th May, 1948 to go fully into the question of profit sharing and to find out a workable formula for a scheme of profit-sharing. The Committee submitted its report on 1st September, 1948.

The Committee has stated, at the very outset that after careful consideration they are definitely of the opinion that as a practical proposition it is impossible to devise and apply such a sliding scale. The main difficulties are that profits

made by industry depend on many factors besides labour, and it may be possible that an undertaking may fail to make any profit in spite of whole-hearted work being done by workers or large profits might accrue in spite of slackness or negligence on the part of labour because of other reasons. Moreover, the measurement of total production in terms of a common unit is a very difficult task and to prescribe a standard of annual production is even more difficult. In view of all these considerations, the committee concluded that labour share of surplus profits can be determined only in a somewhat arbitrary manner.

The committee has recommended six industries, namely, cotton textiles, jute, steel (Main producers), cement, the manufacture of tyres and the manufacture of cigarettes, as sectors in which profit-sharing may be tried in the first instance for a period of five years.

The Committee has defined, (for this purpose) capital employed as paid-up capital plus reserves (including all future allocations of reserves) which are held for the purpose of business. The committee after taking all factors into account, has recommended that six per cent. on paid-up capital plus all reserves held for the purpose of the business would be a fair rate under present circumstances. Besides providing this return on capital, a certain amount of the gross earnings of the concern will have to be provided for depreciation. In fact, the committee states quite clearly that depreciation should be the first charge on gross profits and reserves should be the first charge on net profits, viz., gross profits minus depreciation, managing agency commission, and taxation. While the Committee thinks that a figure of 20 per cent. for reserves should be generally aimed at, as a first charge 10 per cent. of net profits should be compulsorily set aside for reserves. After making all these provisions for depreciation, reserves, return on capital and also fair wages, the surplus that would remain in the earnings of the company would be regarded as the profit to be divided between capital and labour. The labourer's share would be 50 per cent. of these surplus profits. The individual worker's share of profit should be in proportion to his total earnings during the preceding 12 months, minus dearness allowance and any other bonuses received by him.

The Committee has also examined very carefully the question whether labour's share should be distributed by each undertaking, or by each industry or industry as a whole in each region or for all industrial undertakings in the country. The committee's recommendation is for the distribution of profits on a unit basis as a general rule. But an exception, however, has been allowed in the case of textile industry where profit-sharing on an industry-cum-locality basis should be tried out in Bombay, Ahmedabad and Bhopalpur.

It should be noted that all discussions on profit-sharing may be viewed from three important angles, namely, (1) profit-sharing as an incentive to production, (2) profit-sharing as a method of securing industrial peace, and (3) Profit-sharing as a step towards the participation of labour in management. While

labour organisations are disposed to attach the highest importance to the last consideration, the Committee regards it more as a political than an economic issue. On the second point, the Committee think that giving labour a share in the profits of industry, apart from wages, would create psychological conditions favourable to the restoration of industrial peace. This, in turn, will be an important indirect means of facilitating increased production. On the first point, the Committee's view is that by distributing the share of labour among individuals in proportion to their total earnings in a preceding period, a measure of individual incentive to labour for increased production would be provided.

Minimum Wage. Along side collective bargaining, there has been growing of late a movement whereby workers are, all over the world, demanding a 'fixed minimum wage'. It is now well-recognized that in the interest of social justice, wages of the workers must be sufficient to ensure the worker a reasonable and fair standard of living from the view point of the health and general well-being of the employee. 'Sweating' of labour is now considered as unjust, and public opinion is fairly enlightened today to prevent social wrongs. All over Europe minimum wages legislation has the statement of the Pope in which he observed: "Self-preservation is really the duty of one and all and it is a crime not to fulfil it. From it necessarily arises the right to procure all those goods whereby life is sustained and the poor can procure them in no other way than by wages for work. Let it be granted that the workman and his master may freely make agreements, especially as to the amount of wages, nevertheless there is an underlying principle of natural justice, greater and over than any desires of contracting parties, to wit, that the wage must be sufficient to support a steady and frugal workman. For if the workman compelled by his needs is influenced by fear of worse evils, agrees to harder terms, which he must unwillingly accept because the master or contractor so insists, he becomes the victim of force—that justice condemns." (Leo XIII—Pope 1891).

The above observation of the Pope must have had its influence, and in 1928 International Labour Conference adopted a convention in this connection. In our country the question has been examined by several Commissions and Committees, though so far nothing tangible has come out. The Royal Commission on Labour examined the proposal and suggested an investigation into the feasibility of setting up a minimum wage fixing machinery in certain industries before legislation could be undertaken. In 1937, the Bombay Textile Labour Inquiry Committee studied the question of a living wage and recommended an immediate increase in wages on a sliding scale ranging from 3 as. in the rupee on a wage of Rs 13-8 to an anna in the rupee on a wage of Rs. 75 per month. The Cawnpore Labour Inquiry Committee recommended a minimum wage of Rs. 15 per month.

The Minimum Wages Act, of 1948 is a landmark in the history of labour

legislation in India. Since the Payment of Wages Act, 1936, no step so far-reaching as this has been taken by the Government in India.

The main provisions of this Act are more or less the same as of the original Bill which was circulated in 1946 amongst various trade union organisations and employer's associations with a view to eliciting their views thereon. As in the original Bill the Central and the Provincial Governments have been empowered to fix minimum rates of wages or to revise such wages periodically in respect of scheduled employments. The term 'scheduled employments' at present will include employment in woollen, carpet making or shawl weaving establishments, tanneries and leather manufacture, rice mills, road and building construction, public motor transport, lac and mica works, farm labourers and employment in dairies and poultrys. But this list is only illustrative and not exhaustive and can be added to by the Provincial Governments.

The machinery for wage fixing is elaborate and comprehensive. To determine the minimum wages, the Provincial Governments shall appoint advisory committees and sub-committees. The Central Government will also appoint a Central Advisory Board to advise generally on wage-fixation matters and for co-ordination the work of the Provincial Advisory Boards. The Act also contains some penal provisions to prevent payment of lower wages than the minimum fixed.

The main object of this Act is to step up production and increase the wealth of country by creating a contented labour force which is a pre-requisite to attaining the object.—The human element in production, being more important than all others, such a measure was needed for promoting physical and moral welfare of workers. The Labour Minister rightly remarked that if an industry was essential to the community, but could not afford to pay minimum wages it was the duty of the Government to subsidise it and that in no case should an industry be allowed to subsist on the exploitation of the working class.

There can be little doubt that in a country like India with a level of wages that cannot even be regarded as adequate to the needs of physical existence and where labour organisation is still in infancy, minimum wage legislation with a proper machinery to adjust wages to changing prices, is an effective method of improving the conditions of workers. The great danger of minimum wage is that it tends to become a maximum wage. The other difficulty is that this minimum wage must of necessity differ from place to place in accordance with cost of living and other influencing factors.

The application of minimum wage legislation to farm workers is even a more difficult task. The employers are mostly small owners, scattered all over the country, and the labourers are even more scattered and unorganised for any proper scrutiny by an inspecting authority. The agricultural earnings are so varied in amount and made up of such diversified payments, that it would be extremely difficult to fix uniform rate. Moreover, unless the wages

are adjusted to levels of rents paid to landlords and reasonable prices for agricultural produce assured, the measure would be unfair to the mass of petty employers. It is necessary, therefore, to divide such Province into different regions from the viewpoint of wage fixation and to fix rates accordingly for various regional units.

The determination of basis of fixing minimum wages is the next important problem. The minimum wages may be determined with reference to the three main principles, namely, the principle of 'living wage' the principle of 'fair wage' and the principle of wage 'what the trade can bear.' It may be noted that the laws and practice in the U. S. A., Canada, New Zealand and in Australia are mostly based on the 'living wage' principle which is endorsed also by the recent Nehru Committee Draft Report on economic programme and policy of the Congress. All these three principles should go into the determining of a *fair minimum wage*, which must be real and not nominal and must form the cornerstone of the Indian wage structure of tomorrow.

Social Insurance. The idea of social insurance or social security briefly is that state shall make itself responsible for ensuring a minimum standard of material welfare to all its citizens, on a basis wide enough to cover all main contingencies of life of an individual from birth to death. It includes security when a man is employed as well as when he is unemployed or destitute.

The second half of 19th century witnessed a remarkable teaching, specially in Germany of the increased activities of the state. In the eighties of the last century Germany introduced social insurance, which comprised compulsory insurance of sickness, accidents, old age and infirmity. This was soon followed by Denmark and Britain. In England in 1909 the Old Age Pensions Act was passed followed by Health Insurance Act 1911-24, Unemployment Insurance Act 1920-31, the Widows', Orphans', Old Age and Pensions Act 1925-32 for insurance against loss of health. Thus examples of state action and the discrediting of *laissez faire* doctrine may be seen in the subsidy to wages in the form of old age pensions, health and unemployment insurance, education, hospitals, maternity benefits and child welfare.

The new step in the evolution of the system operating in England is the introduction of Beveridge Plan, which is a comprehensive scheme of social insurance, covering the entire population and ranging from maternity benefits to funeral grants. The new scheme is an outstanding advance, since in place of previous unsatisfactory patchwork, it makes adequate provision against all major social evils on the basis of social minimum. The Beveridge Plan is a plan for the security of incomes for every man, woman, and child in the community. All the contingencies of life and livelihood, birth, marriages, old age, death, unemployment, accident, illness and disease are covered by a

single and comprehensive system of contribution under state auspices. Under the scheme every one pays and every one receives. In short, a man and his family are to be insured in respect of all eventualities which either cause an interruption in earnings or an exceptional increase in expenditure. The whole scheme is now studied all over the world as an example of what a progressive Government can do in the direction of providing for social security.

Social Insurance in India. We have no social relief laws in India—except perhaps a few which were born dead or have long since been ineffectual. The state in India has scarcely yet deviated from the traditional policy of *laissez faire* in this respect. The famine relief measures can not be described as ensuring social security; these are measures of humanitarian relief meted out to actually starving population in the event of acute shortage of food. The Workmen's Compensation Act and the Provincial Maternity Benefits cover only a minor part of the distress of the industrial worker which again is a small section of our population. As far back as 1927 the International Labour Conference adopted a draft convention on the subject of sickness insurance by imposing on the States an obligation to set up a system of compulsory sickness insurance. The convention was not ratified by the Government of India and sickness insurance never became a reality. In 1933, the International Labour Conference adopted draft conventions regarding invalidity, old age, widows' and orphans' insurance. The Government of India, however, refused to ratify these Conventions on grounds of financial and administrative difficulties. The question of old age insurance was also raised in the Legislative Assembly in 1937. The Government once again refused to give the proposal any serious consideration.

The necessity of social insurance in India is urgent and we cannot afford toying with the problem. The deteriorating conditions of the lower classes of our population, the growth of the socialistic spirit, and the schemes evolved in other countries, have made us realise that something must be done to ameliorate the condition of our masses. Social insurance shall provide us with adequate remedy for many of our social ills. It can be an excellent income maintenance device and will surely raise the standard of living of the labourers; while at the same time benefit employers by tending to solve the problem of labour scarcity, instability, turn over and absenteeism.

The whole problem is beset with a number of difficulties,—financial and administrative, and others such as the immensity of population, its phenomenal poverty, the lack of reliable data, the primitive character of sanitary measures and the absence of an effective public opinion, conscious of the claims to a full human life. Indian labour is still migratory and unorganised, illiterate and ignorant; their wages are still so low as to render them unable to make contributions to any scheme of insurance.

Beginning must be made however. It does not mean that we must imitate the Beveridge Plan for adoption in our country. Such comprehensive

scheme would be beyond the dreams of the wildest imagination. We can begin with one aspect of the scheme, only we must have a unified system. Difficulties must be surmounted. Lack of statistics is certainly a great hinderance but an attempt to work out a scheme will itself open out possibilities of making statistics available. Mr. A. N. Agarwala in his excellent book 'Social Insurance Planning in India' pleads for "the introduction in our country of one branch of social insurance after another, according to a pre-determined schedule and pattern, so that while we may implement only one branch at a time and one after another according to our resources and requirements, every new branch which is called to life does not follow its own path and contribute to a haphazard and asymmetrical growth but occupies its own place in the harmonious and rhythmical pattern drawn up in advance and to be realised at the end."

In the existing circumstances the sickness insurance is the most desirable and feasible beginning. A suitable and workable sickness insurance scheme was prepared and submitted by Professor Adarkar to the Government of India. The health insurance scheme, which involved three years of preparation, took concrete form in the shape of the Employees' State Insurance Act.

The Employees' State Insurance Act was passed by the Dominion Parliament on 2nd April 1948, and the Employees State Insurance Corporation was inaugurated by the India's Governor-General on 6th October 1948.

The scheme will apply in the first instance to employees in factories other than seasonal factories. This comes to about 2 million employees only. It is thus a modest start but may, as the Labour Minister claimed, well prove to be the corner-stone of a great edifice which a free country seeking its economic salvation must build.

Contribution is payable by all employees to whom the Act applies, and who are classified under 8 categories on the basis of their average daily wages. The amount payable weekly, ranges from 2 annas in the case of those whose average daily wages are between Rs. 1 and Rs. 18.0, to Rs. 14.0 in the case of those whose daily wages are Rs. 8 and above. The Employers' contribution works out to double that of the employees in each category except in cases where the daily average wages are below Re. 1 and also in cases where the daily average wages are between Rs. 1 and Rs. 18.0, the employers' contribution in these cases being fixed at 7 annas.

The Corporation is to get from the Central government during each of the first 5 years a grant equal to two-thirds of the administrative expenses (not including the cost of the benefits). In addition it may also accept grants, donations or gifts from Central or Provincial Governments, Indian States, local authorities and institutions and individuals. The preliminary expense incurred by the Government in connection with the establishment of the Corporation will be treated as a loan and adjusted against grants to be made by the Government to the Corporation.

Briefly the scheme provides four types of benefits, namely, (1) sickness

benefit payable for not more than 56 days in any continuous period of 365 days at the rate of half the average daily wages, (2) medical benefit either in the form of outpatient treatment and attendance in a hospital or by visits to the employee's home, (3) maternity benefit at the fixed rate of 12 annas per day for a total period of 12 weeks and (4) disablement and dependants' benefits at fixed weekly rates in lieu of compensation or damages payable under the Workmen's Compensation Act. The Corporation may, at the request of any Provincial Government, extend medical benefit to the family of an insured person also. The provision of medical benefit will be the responsibility of the provinces concerned and, where the amount of sickness benefit payment in any province is found to exceed all-India average, the amount of such excess will be shared between the Corporation and the Provincial Government by the agreement.

The Corporation is to consist of representatives of the Central Government, Provincial Governments, employers and employees, the medical profession and the Central Legislature. From among these representatives, a standing committee is to be appointed, and this committee will be in charge of the administrative affairs subject to the general superintendence and control of the Corporation. A medical benefit council, to be constituted by the Central Government, will advise the Corporation and the standing committee on matters relating to the administration of medical benefit. The Corporation may also promote measures for the improvement of health and welfare of insured persons and for rehabilitation and re-employment of insured persons.

Labour Legislation in India

The labour legislation in India is essentially a product of 20th century, several labour acts were in existence before also. The chief characteristic of the enactments that were made in the 19th century was that they were not for the protection of labour, but in the interests of employers—foreign or Indian. The earlier Assam Labour Acts, the Workmen's Breach of Contract Act 1859, the Employers and Workmen's (Disputes) Act 1860, were all conceived in the interests of the employers with a view to supply them with a docile labour force. The rapid development of cotton industry in Bombay however, began to cause alarm to Lancashire, and the prevailing abuses in connection with child and women labour in Indian factories were the grounds on which the Lancashire interests insisted on India to enact labour laws—not intended in the interests of workers but to restrict the profitableness of Indian industry, and this finally culminated in the factory acts of 1881 and 1891.

Factory Legislation The Act of 1881 applied to factories using power and employing more than 100 persons. It required the minimum age of 7 years for children, and the children between 7 and 12 could work only 9 hours a day with an hour's daily rest and with 4 holidays in the month. The application of the 1891 Act was extended to factories employing 50 persons. The age of the working children was raised to 9 and 14, while the maximum working hours were reduced from 9 to 7 per day. It protected women and children against

night work and fixed a maximum of 11 hours a day for women workers.

On the basis of recommendations of labour commission appointed in 1903, a new Act was passed in 1911. It limited the hours of work to 12 in the day for men and to 6 in the day for children employed in textile factories. Night work was forbidden except in certain cases and seasonal factories were brought under control.

The exigencies of the war 1914-18 made it necessary to increase production and some of the restrictions of the Factory Acts were temporarily removed during the war. In 1922 another Factory Act was passed. This applied to all power using factories employing not less than 20 persons. The hours of work for all adult workers were restricted to 11 in any one day, and 50 for a week. The minimum age of working children was fixed between 12 and 15 years. Provision was also made for health and safety of workers, better sanitation and effective inspection.

The act was further amended in 1934. The working hours for adults were limited to 54 a week or 10 a day. The act provides for a weekly holiday, rest periods and for certificates of fitness for persons between 12 and 17. It also lays down that no child between 12 and 15 shall work for more than 5 hours a day. The principle of spread over was applied for the first time. Artificial humidification measures were expanded, and provisions were laid down for welfare of workers and overtime work.

A landmark in the history of labour legislation in India, was the amendment to the Factories Act 1934, providing for the reduction of the maximum weekly hours of work from 54 to 48 in perennial factories and from 60 to 50 in seasonal factories. The 'spread over' has been reduced from 13 hours to 10 hours in case of perennial factories and 11 hours in case of seasonal factories. The amendment at the same time empowered Provincial Governments to exempt any industry from this provision. A noteworthy feature of the Act is that it provides for the payment of overtime work both in perennial and seasonal factories and increases its rate to double the rate of worker's pay in order to discourage working overtime in factories. The Act came into force from 1st August, 1946. In fact, the reduced hours will result in greater productive efficiency.

The Factories Act of 1948 takes the place of the Factories Act of 1934 and came into force on the 1st day of April 1949. This new Act will be applied to all the Provinces and to such of the States as have acceded to the Centre in respect of labour legislation. The Act is not in any sense a revolutionary measure, but it contains a number of important amendments and new provisions which invest it with a certain amount of special significance.

The scope of factory regulation has been considerably widened by the new Act. The existing law applied only to industrial establishments where manufacturing process is carried on with the aid of power and where twenty or more persons are working. The new Act becomes applicable to all factories

employing ten or more workers where power is used and to factories employing twenty or more workers where power is not used. The new Act has also abolished the distinction which was made in the old Act between seasonal and perennial factories.

In order that the initial planning and lay-out of factories may be carried out in a satisfactory manner provision has been made for the compulsory registration and licensing of factories by the Provincial or State officials concerned, and for prior sanction for the construction and extension of any factory.

So far as the working hours are concerned no adult worker will be required or allowed to work in a factory for more than forty-eight hours in any week. On any particular day an adult worker will not be required or allowed to work for more than nine hours. No worker will work for more than five hours before he has had an interval for rest of at least half an hour. Inclusive of the intervals for rest the spread-over of the total working period of a worker in any day must not exceed ten and a half hours. For overtime work the worker would be entitled to wages at the rate of twice his ordinary rate of wages. A holiday for a whole day in every week is assured to the workers. In case of women workers, it has been laid down in the Act that no woman should be employed in any factory except between the hours of 6 a.m. and 7 p.m.

While the existing legislation left too much to the rule-making powers of the Provinces, the new Act lays down minimum requirements in respect of the health, safety and general welfare of workers, thus limiting the powers of the Provinces and States to making rules for the less important procedural matters. The Act also places the responsibility for ensuring the compliance with the provisions of the Act on the occupier of manufacturing establishment and not on inspectors as provided for in the existing legislation.

Other provisions include (1) the fixation of daily and quarterly limits of overtime, the raising of annual leave with wages from 10 days per year to one day for every 20 days of work in the case of an adult and to one day for every 15 days in the case of a child, (2) the raising of the minimum age of children in the factories from 12 to 13 and reduction of their working hours from 5 to 4½ with powers to Provincial Governments to prescribe higher limits in the case of hazardous undertakings.

The Act has also provided that in every factory wherein five hundred or more workers are ordinarily employed the occupier will employ in the factory such number of welfare officers as may be prescribed.

Mining Legislation. The first mines Act was passed in 1901 and it provided for appointment of inspectors. The act was amended in 1923 and provided for a weekly holiday, for the limitation of hours of work for adults above ground to 40 a week and under ground to 54 a week, and for the prohibition of employment of persons below 13 years of age. In 1929, regulations were made to exclude by stages women from work underground. The 1930

was further amended in 1935. Employment of children below 15 years of age was prohibited. The hours of work were limited to 51 per week, and 10 hours a day above ground and 9 hours a day under ground. The provision relating to employment of women under-ground was suspended during the second world war but has again been resorted after the cessation of hostilities.

Indian Mines Amendment Act was passed in 1946. It empowers the Central Government to require colliery owners to construct locker rooms and bathing places with shower baths separately for men and women employed in their mines and to maintain them according to prescribed rules and standards. Since then, the Coal Mines Pithead Bath Rules have been framed and published by the Government of India.

Coal Mines Provident Fund and Bonus Schemes Act, 1918 has given powers to the Government to prepare and introduce these schemes in the first instance in coal mines as an experiment and then, in due course, to extend to other industries also, with suitable modifications. While the provident fund scheme is still under preparation, the Government have gone ahead with the bonus scheme. In coal mines today about 90 per cent of the workers are casual labourers. It is therefore difficult to introduce the provident system at once. But Government is determined to introduce it and it was proposed that the employers should contribute a sum equal to one anna in the rupee of the basic earnings and the workers should also contribute a similar amount.

Transport Legislation The railway workshops were covered by the Indian Factories Act of 1923 but the other railway workers were not protected by any legislation. Government of India had already ratified the I. L. O. Convention in this respect. In 1930, Indian Railways (Amendment) Act was passed which limited the hours of intermittent work to 81 a week and non-intermittent work to 60 hours a week, and provided for rest and inspection.

As regards maritime labour, the Indian Merchant Shipping (Amendment) Act 1931 insists on a minimum age for admission of children to employment at sea and for admission of young persons to employment as trimmers and stockers, provides unemployment indemnity in case of loss or foundering of the ship, and requires medical examination and a certificate of physical fitness for children and young persons. Provisions are laid for protection of the seamen's rights, protecting dockers against accidents in loading and unloading. Child labour has also been regulated. The Children (Pledging of Labour) Act of 1933 has been passed to abolish a particularly revolting form of child slavery.

Other Legislation. Social rights of the workers have also been considered, and the Workmen's Compensation Act was first passed in 1923. Since it has been kept up-to-date by subsequent amendments from time to time providing for changing conditions. The provision has been made for compensation when a worker meets an accident or contracts some occupational disease. Maternity Benefits Acts to meet one of the urgent needs of women workers

have been passed by the Central Government and also some of the Provincial Governments, the Bombay and U. P. governments being the leading ones. Payment of Wages Act, 1936 is perhaps the most difficult piece of social legislation passed in recent years. It lays down very elaborate and detailed regulations regarding imposition of fines on the workers, deductions of various kinds from the wages, the payment of wages and as to the time and mode of payment.

Industrial Employment (Standing Orders) Act was passed in 1916. It applies to all industrial establishments employing 100 or more workers in British India. It makes it obligatory for the employers of such establishments to define conditions of service such as wage rates, conditions of leave and holidays, termination of employment, suspension or dismissal for misconduct etc., and get them certified by an officer appointed for that purpose by the Central or Provincial Governments as the case may be. This Act aims at avoiding vague and ill-defined terms of service in industrial establishments. In the conciliations and arbitration of industrial disputes, standing orders as certified under the Act, will be very useful to judicial authorities.

Protection has also been afforded to labourers employed in shops, hotels, restaurants etc. Shops and Commercial Establishments Acts have been passed by Provincial Governments to give relief to such labourers. Provision has been made for the limitation of hours, rest, holidays etc.

It is not considered necessary to refer here to other legislative measures, such as Trade Disputes Act, Trade Unions Act and plantation legislation, which have been described and commented upon at their appropriate places.

It is evident from the above that in recent years there has been a crop of labour legislation. It should not, however, lead one to suppose that nothing remains to be done in future. There are still problems which remain untouched and unsolved. In case of small establishments the working conditions are most unsatisfactory, and often bigger establishments are split into smaller units to evade the application of law. The inspection and administration of the legislation still leaves much to be desired in order to get the fullest benefit and use of the various measures that have been taking during past years.

Industrial Welfare

Industrial welfare work was originally defined as "anything for the comfort and improvement, intellectual or social, of the employees, over and above wages paid, which is not a necessity of industry nor required by law." The scope of study was thus laid "entirely separate and distinct from other phases of employment. Wages might be low, hours long, working conditions bad and tenure of employment insecure, but if the establishment had, before correcting these evils, installed a good lunchroom, wash rooms or other welfare features, it was scheduled for that." This view is now gone, and today welfare work includes provision of amenities and facilities for the workers both within and without the factory. Not only that, welfare work at

present means work undertaken for improving the health, safety, general wellbeing and industrial efficiency of the workers beyond the minimum standards set up by the Factory Act or demanded by the pressure of organised labour. The term is thus used to designate 'the voluntary activities of employers to secure for their work people good working conditions inside the factory and to provide, outside the factory, facilities for recreation and other amenities of life that contribute to their wellbeing.' Emphasis is laid on the voluntary activities, legislation secures statutory welfare.

It must be admitted that there is a close connection between statutory and voluntary welfare. The former is necessarily limited in scope and relates to special requirements necessitated by the nature of occupation while the latter relates to the general welfare of the workers. Law can lay down only minimum standards. But well-conceived legislation furthers voluntary work, and a high standard set up by good employers makes way for their inclusion in future legislation.

Welfare work is only a recent innovation which took deep roots after the First World War. Industrial Revolution completely changed the relationship between the worker and the master. There was left no other contact between them except "the nexus of naked self-interest and callous cash payment." As the size of the business grew, personal contact between the employer and workers gradually disappeared. In absence of this sustaining influence, the relations between employers and workers were embittered, because of the fact that complaints went unheard, grievances unredressed, and resort was taken to direct action. The growing tension and friction between labour and capital, pressure of public opinion, sense of social equity all impelled action. Until the war, it was hardly thought of owing to the ignorance and apathy of worker himself, shortsightedness of employers, the neglect of the state and indifference of the public. The war with all its attendant revolutionary circumstances helped to give a new perspective to these problems of workers. It became obvious to everyone thinking seriously about industrial life that efforts should be made to sustain their health and powers of endurance, improve their mental alertness, develop their individuality and enlarge their capacity for sound citizenship. It is with a view to solve these problems and to restore human touch to the industry that welfare work is necessary.

The need for welfare work in India is greater. Indian labour is migratory and extremely inefficient. To secure a stable and contented labour force, to minimise labour turnover, conditions must be improved, and much can be done through welfare work. If a benefit in form of increased cash wages is given to the Indian worker, it may not have the desired result on his efficiency. He may take to increased gambling, drinking or extravagance. If, on the other hand, his condition is sought to be improved through welfare work, his efficiency is bound to increase. He shall be made to feel the need for self.

improvement, and then make efforts to secure it. Absence of well organised trade unions in our country which could look after the interest of workers, lays emphasis on the need of welfare work in India.

Welfare work in business and industrial enterprises is that part of the management concerned with organisation of working conditions on such lines as will be acceptable to, and provide for each individual worker (a) physical comfort and wellbeing (b) full opportunities for the use of his work and abilities; and (c) means for the development of all his faculties. It aims at assisting the individual to fulfil his function both as a citizen and producer in the interests of the community as well as of the particular enterprise with which he is connected. It seeks to promote a better understanding between employer and employee based on just dealing and mutual co-operation.

The objects in short are: (a) humanitarian since its purpose is to enable the workers to enjoy a richer and fuller life; (b) partly economic in that it is meant to improve the efficiency of labourer, to increase its availability where it is scarce, to secure a better class of workers and to keep them contented so as to minimise the inducement to resort to direct action, and (c) partly civic in that it aims to develop a sense of responsibility and dignity among workers and thus pave the way to their becoming independent minded and useful citizens by providing them with adequate recreational, technical and educational facilities.

One thing must be emphasised. Any schemes of welfare should not be taken out of mere pity or philanthropy. They are looked upon with suspicion and even antagonism by trade unions. This sort of feudal charity is resented by self-respecting workers. What is needed is to organise welfare work as a part of efficient organisation and management, in which adequate care and attention is given to the needs and problems of the workers. The work should engender a feeling of a changed mental attitude on the part of employers recognizing the claims of and with a view to secure efficiency for the workers.

The welfare work may be administered by the employment department or in large concerns by a committee consisting of management and workers. No scheme can be devised which can be equally well-applied to all undertakings. Each concern has its special problems to solve which a suitable policy should be evolved, considering its size, requirements and resources. For the success of the scheme, it is extremely essential that the scheme shall be worked with co-operation from all sides—management, workers, foremen and other executives with a unity of purpose and in complete harmony and with a feeling that they have a sacred obligation towards their fellow workers and to the society at large. Schemes once evolved should be entrusted to the workers and they should be required to give their willing co-operation and living interest in details of work. Management should confine itself to broad outlines of policy; too much interference on their part kills the initiative of the workers, and many a scheme result in failure.

As to what activities should be included in welfare work is a matter to be decided with due regard to the nature and location of the industry, the size of undertaking, the type of work involved and the system of organisation. Broadly speaking welfare work may be divided into two classes—work inside the factory and work outside the factory. Arrangements within the factory may include such activities as reorganisation of recruitment system; rate fixing, rules regarding leave, promotion, transfer, dismissal, and holidays; standardisation of wages, proper lighting, cleanliness, ventilation, maintaining of proper temperature, organising rest pauses, time, motion and fatigue studies; provision of technical training, prevention of accidents and noise, and such other facilities as mess rooms, cloak rooms and lavatories. Of the work outside the factory, provision of general and technical education, provision of cheap rent and suitable housing accommodation, free medical aid, cheap credit facilities and social insurance and thrift schemes are the most important. Facilities may be provided for hearing the complaints of workers, their ready and prompt adjustment, for letter writing to friends and relatives and also facilities for remittance of money to their dependents.

Recruitment The various evils associated with the recruitment of factory workers in India, and their harmful influences on the efficiency of workers have been already discussed. In the interests of efficiency and in order to secure a stable labour force it is essential that these evils must be removed. The recruitment should be made in a scientific manner. Removal of the jobber shall save the worker from the clutches of the money lender and other parasites. Suitable selection tests must be evolved, and the persons formerly employed else where, must be required to produce certificates from previous employers. Nepotism should be discouraged and sheer merit must be the deciding factor. After his selection, the worker must be familiarised with the nature of his work and duties. He may be shown round the factory, introduced to his fellow workers and to the officers under whom he has to work. Rules about factory discipline and routine must be explained to each worker on engagement, and if possible a printed copy thereof should be supplied to him. Proper arrangements and rules should be made regarding holidays, leave with or / and without pay, promotion, transfer and dismissal, etc. Arbitrary fines or deductions from wages should be discouraged. Proper records must in all cases be maintained of the work of every employee and their progress must be closely followed during their stay in the undertaking. Periodical tests may be organised to consider the question of promotion or dismissal. Workers must however be convinced that there shall be no arbitrary or unjust dismissals. Security of employment is an important contributing factor towards harmonious relations. Lastly public employment exchanges may be set up. It will minimise aimless migration in search of work.

Cleanliness and Ventilation, etc. A high standard of cleanliness and tidiness, and maintenance of hygienic conditions within the factory is highly

desirable. The factories should be periodically white-washed. The lighting system should be carefully designed so as to give abundance of even light suitable to the needs of the workers. Dim, dazzling and glare lights impede working, cause headache, prove injurious to the eyes of workers and cause accidents. Factory and workshop should be properly ventilated. Temperatures should be maintained at proper levels to ensure comfort and well-being to the worker. In textile mills, artificial humidification schemes must be wisely conceived and properly administered so as to cause the least inconvenience, injury or discomfort to the workers.

Bath and Toilet Facilities etc. Bathing is extremely necessary in Indian climate, and therefore any facilities provided by employers in this respect are much appreciated by the workers. Conditions regarding this are very unsatisfactory in Indian factories. Bath rooms, washing facilities, and lavatories should be provided. Fresh drinking water should be available in sufficient quantities. Dining rooms and cloak rooms are other items in this connection. There should be available clean and neat places where workers can take their meals during intervals and can take rest. Partaking of meals, freshly cooked and at reasonably low prices amidst cheerful surroundings in company with others would stimulate healthy fellow-feeling and would act as a source of mental and physical relaxation. If possible cheap tea-stalls and restaurants should be set up where the workers can refresh themselves without much expense.

Establishment of Creches. It is an institution where the young children of women employees are taken care of whilst the mothers are at work. A trained nurse should be kept to look after children. Children here are saved from the foul air; dangerous fumes and accidents to which they are exposed if they accompany their mothers to the machines. Undertakings employing large numbers of women workers must provide these facilities, as they have a direct and very important bearing upon children's health. It is regretting that conditions in this respect in our country specially in Bengal are very unsatisfactory, though some of the Bombay and Ahmedabad employers have done really good work.

Prevention of Accidents. Self-preservation is the primary consideration of individuals. It must therefore be seen that workers are not exposed to any danger. Dangerous machinery should be adequately fenced. Mechanical safety devices, like fire extinguishers, should be installed, and where necessary, protective clothing should be supplied to the workers. Safety measures should be taught to the ignorant and inexperienced workers, if necessary through posters and charts. Safety aid boxes must be kept in readiness and trained doctor for emergency cases must be employed.

During times of war, when workers are in places exposed to enemy action, proper arrangements must be made for their safety. Bomb proof shelters, safe in quality and good in number, must be provided. Workers should be given

sufficient practice as to their behaviour during air raids. The question of motion and fatigue study may be taken up and suitable rest pauses may be evolved. Hours should not be unduly long. Exhaustion due to over work and consequent physical and mental strain leading to illness should be avoided. It is highly desirable that proper shift systems are arranged. Night work, unless indispensable, must be discouraged.

Education Provision of education is one of the most important services that the employers can render to the workers. The Indian worker is known for his ignorance and therefore workers' children hardly get any encouragement from their parents for education. On the other hand, the children may be asked to work in the factory in order to augment the family income. The supply of educational facilities is usually not a directly paying proposition. But it has important, wholesome effects on the efficiency of the workers. More literacy may not bring about much difference in the technical competence of the workers, but it makes a great difference in their understanding. Literacy would thus materially help not only in the acquisition of simple technical knowledge, but also in proper understanding of other matters. Number of strikes in India take place because of the ignorance and lack of judgment on the part of the workers. They are easily exploited by outsiders often for their personal ends. If ignorance is removed, employers will be able to secure intelligent body of workers who will not allow themselves to be used as pawns in the personal or political game of interested outsiders. Almost all big undertakings have provided facilities for some sort of education, but they are far short of the need. Primary education must be compulsory, and to liquidate illiteracy on a large scale, adult education may be provided for. A sound elementary education is sure to help in creating a civic sense and in turning out a more efficient class of workers with a better and more hopeful outlook on life.

Food and Nutrition The food that a worker consumes depends very largely on his income, and as wages are low, the kind of food taken by vast majority of Indian workers is poor. It is essential to give them the proper kind and amount of food necessary for health and strength if their efficiency is to be maintained. Wholesome food must be available at cheap and moderate cost to the workers. The soaring war time prices require the provision of grain at the minimum rates. Cost price grain shops may be opened and this work can very well be taken up through co-operative societies. The middleman should be prevented as much as possible from fleecing the consumer. A cheaper supply of sugar and protective foods such as vegetables, fruits and milk should be arranged for the workers. State can help in this through readjustment of central, provincial and local taxation. At present our taxation system is rather regressive, incidence of taxation is specially heavy on commodities of common consumption by the poor, as food grains, firewood, kerosene, etc.

Housing. There is a close connection between health, housing and sanitation. In almost all big industrial towns of India, conditions regarding

housing accommodation are most deplorable. A low wage combined with high rents compels the worker to reduce his expenditure in other direction, i.e., food and nourishment. Injurious effects of bad and inadequate housing cannot be over estimated. A few sporadic and ill-conceived attempts were made to solve the problem but they failed. Attempts have also been made at several places by a few employers. But in these cases, accommodation is available almost invariably on the condition that the worker shall not owe allegiance to the trade union, and shall not take part in strikes. If they do so, they are turned out; and at times of strife the lot of the workers generally becomes pitiable. In many cases therefore the accommodation provided by employers is not availed of. What the workers want is good and strike free houses with cheap rents and a sense of security so that in times of unrest they shall not be at the mercy of the employers liable to be thrown any time on the streets. Reliance cannot be placed on private estate agents or speculative builders. Its solution involves a well-thought out and co-ordinated plan of house construction and slum clearance undertaken by employers, and, if necessary, helped by the state. It may be mentioned that houses can be constructed in suburbs outside the town, and employers may provide cheap, quick and efficient transport to the workers from and to the mills. In this way workers can live at a distance in better surroundings and comparatively cheap rents. Cheap bus services may be introduced between labour settlement and factory areas by employers or state.

Medical aid. Nothing so much directly affects the efficiency of the worker as his health. In order to protect his health, provision of free medicines and attendance is the chief requirement of the worker. For, though family budget statistic reveal a little money sometimes spent by workers on medical treatment, the amount they can spare is so small as to be of little benefit at the existing prices of medicines and medical attendance. A considerable part of absenteeism in Indian factories is due to ill-health of the workers. No estimate can be made of loss of income to the workers and the loss to the industry due to incidence of disease, largely of preventible character.

Although provision of facilities in this respect seems to be practically universal or at least in larger establishments in India, but efforts made so far have been able only to touch the fringe of the problem. Dispensaries have been set up but they are not well-kept. In most cases there are no qualified whole-time doctors or at best the visit of the doctor is periodical. Charge is generally nominal but the workers do not seem generally to appreciate the advantage. It appears that there is something radically wrong with the present state of affairs. It is alleged that doctors don't take any interest in their work and that they are employed not for the welfare of the workers but to be used as instruments of tyranny and abuse. Before a worker is given leave on medical grounds, he is required to produce a medical certificate from the mill doctor. The mill doctor, unless the case is very serious, refuses to give the certificate. Cases have been brought to notice where deaths have occurred within few hours

of the refusal by the doctor to give a certificate of illness.

What is required is that medical attendance should be free or on nominal cost. Properly qualified *wholetime* doctors are the urgent necessity. The doctors should be courageous enough to withstand any pressure brought to bear on them with a view to harrass the workers. The number of hospitals should be increased and they should be well-equipped with medicines, apparatus and trained nurses, compulsory and contributory sickness insurance scheme would be extremely helpful in Indian conditions.

Recreation. To counteract the effect of stuffy atmosphere and congestion, and day's fatigue, provision of amonities for mental and physical recreation has an important place in welfare work. Holidays with pay are important in this connection as they afford the labourer the necessary break in strain and monotony of continuous industrial work. Indoor and outdoor games should be provided. Arrangement for physical exercises and sporting activities may be made. Emphasis should be laid on indigenous games and sports such *Kabaddi* and wrestling matches. Sporting activities, exhibitions, matches, *khafan* and *quawal* parties, are much appreciated by Indian workers. Picnic, excursions and outings may be arranged. Dramatic society social and literary clubs, debates and discussions, musical entertainments should be organised to raise their aesthetic and intellectual interest and development. Cinema shows and exhibitions may be organised for displaying topics of interest such as health and sanitation, etc. Provision of playing fields for children, parks, libraries and reading rooms and other recreational facilities are the responsibility of the employer.

Development of thrift etc Habit of thrift may be inculcated in the workers. Extravagance should be discouraged. Schemes of contributory provident fund may be set up. Any bonus or provident fund schemes must be, however, free from encumbrances. It is alleged that in some cases payments under these schemes are paid on the condition that the worker has placed in a certain period of satisfactory continuous services, and if they are found taking part in strikes or organising unions etc, these benefits are forfeited to them. Such disabilities should be removed. Consumers' co-operative stores should be established, and with a debt relief organisation, cheap credit through co-operative societies should be made available. Workers should be encouraged to make small savings wherever possible.

Rationalization and Labour Rationalization consists in the systematic effort to get the most out of the resources—labour and materials employed in various economic activities. Rationalization affects labour in a variety of ways—especially through the changes in the technique of manufacture and labour management. In India these have been called by different names, such as 'rationalization', 'efficiency system', or intensification of labour'.

The aim of all these measures is to reduce cost of production and/or to increase the margin of profits. In so far as it relates to labour, there are two ways in which it can be done: either by reducing the rate of wages, or

by asking them to do more work for the same wage. The first method is rarely successful owing to the stiff resistance of organised labour. Wage cutting is difficult even in a country like India where labour is not well organised. Naturally resort is taken to the other method. Rationalization in this respect is concerned with such things as better selection and training of the worker taking up of time, motion and fatigue study, better organisation of worker and working processes, supply of better tools and instruments with a view to increase the efficiency of the worker. It goes, therefore, without saying that rationalization invariably increases the efficiency of the worker. The effect of these measures may now be seen on other aspects of labour.

Effect on employment. When labour saving machinery is introduced in an expanding industry, the process of installation is generally gradual, and it rarely results in actual displacement of labour. Where such measures are taken in a depressed industry, they lead to direct displacement of labour, and fear of unemployment amongst workers, and that usually at the time of trade depression. Sufficient statistics are not, however, available to determine definitely the relation between rationalization and employment. The extent of unemployment, in any case, is less than one might be led to imagine. Some of the unemployment created in early stages is remedied by improvements in the organisation of industrial undertakings in so far as they lead to better adaptation of production to market needs. The fall in prices leads to increased sales and consequently further production, and reabsorption of a section of those who were formerly displaced. It may be concluded that majority of rationalization measures involve a certain degree of unemployment, though temporary. But as rationalization goes on, it must of necessity lead to a certain permanent margin of unemployment. This may be considered as the price paid for progress. There is a danger here and that is that the new employment may not take place in the country of rationalization, but in some other country. For example, rationalization of transport in India created new employment in foreign countries manufacturing automobiles, locomotives and aircrafts. The price paid in such cases is greater.

Effect on Work Additional strain and fatigue may be imposed on the workmen as a result of asking them to do more intensive work. Employers point out that as material surroundings and general conditions of work are improved, there is better layout of work, better materials and improved tools, there should be no reason for increase in strain. In theory they may be conceded; in practice they are easily solved. The question of time and fatigue study is highly specialised, and needs a number of experts. The industrial engineer, psychologist and physiologist must all co-operate if dependable results are to be obtained. Neither such technicians employed in India, nor they are available. Another difficulty is that even where such experiments are made, they are true of and applicable only to the conditions of the individual undertaking for which they are made. In India the inferences drawn by few were

copied and applied by others in highly different conditions. It goes without saying that on the whole results are beneficial and the above remarks emphasise only the difficult nature of the problem. Many extremely unpleasant tasks are replaced by simple handling of a few levers.

Effect on Wages. A number of experiments show that wages are increased. On the other hand, the general level of wages is linked with technical progress and consequently of spread of rationalization. The wider the field of application of rationalisation, the more are the chances of a lasting increase in wages. A certain rise in wages is often a necessary preliminary to the introduction of new working methods. The worker is provided with articles of improved quality at lower prices and therefore his real wages are increased. But the net effect can be known only after considering the net employment situation.

In the above paragraphs, certain conclusions have been drawn bringing out the adverse effects of rationalisation. It does not mean an embargo on technical progress, that would be suicidal for any country. It only emphasises the fact that serious nature of short term difficulties must be recognized and provided for while admitting the corrective forces and their advantageous nature in the long run. A short term in this case may well cover the life of a whole generation, and we cannot be neglectful of the catastrophic changes that may be brought about in the life of the present generation in consideration of merely possibly beneficial effects to future generations.

Test Questions.

1. What are the various criteria that should be applied in judging a particular wage system? Illustrate your answer fully.

(Rajputana B. Com. 1942)

2. "The industrialist is mainly responsible for industrial efficiency."

Discuss.

(Bombay B. Com. 1944)

3. Why is labour legislation considered necessary? Examine broadly the principal features of such legislation in this country

(Bombay B. Com. 1942)

4. What do you understand by the term 'living wage'? How would you calculate it for textile workers in Bombay City? What would be the likely effects of the enforcement of such a wage? (Bombay B. Com. 1941)

5. What are the obstacles to the efficiency of labour under modern factory conditions? How can these obstacles be surmounted?

(Bombay B. Com. 1941)

6. Discuss the various methods of wage payment to workmen in industrial establishments in India. How far are they conducive to efficiency of labour?

(Bombay B. Com. 1939)

7. Analyse the causes of industrial disputes, distinguishing clearly between proximate and remote causes. What measures would you recommend (1) for settling disputes and (2) for preventing them?

8. 'The principal object of management should be to secure the maximum prosperity for the employer, coupled with the maximum prosperity for each employee.' Discuss this statement fully. (*Allahabad B. Com. 1938*)

9. Distinguish between co-partnership and profit sharing, and discuss the advantages which profit sharing holds out to employees. Can you suggest any practical difficulties likely to be experienced in the working of profit sharing schemes ? (*Agra B. Com. 1942*)

10. Give a short description of the industrial welfare work in India.

(*Agra B. Com. 1944*)

CHAPTER 15

STATE IN RELATION TO INDUSTRY

Gone definitely are the days when the ideas of *laissez faire* dominated the economic world, and the state was considered to be a passive onlooker, to be only in the nature of a 'holder of the ring while the combatants would fight out their differences.' The functions of the state were only three—defence, administration of justice and maintenance of certain public works. The king was a mere war lord, raised to his position solely for military purposes, and with no conceded rights of social or political interference, while the central government was looked upon largely as a war device, or at best, as a means to preserve the freedom of commerce, and not as something which should interfere with social or industrial customs or the freedom of industrial contracts.

It was gradually realised that the widely claimed theoretical benefits of *laissez faire* were not realized in practice, and that it did not necessarily lead to the survival of the fittest. There is a growing conviction in every advanced country that voluntary action on the part of the individual has miserably failed to promote the healthy economic development of the country and the time-honoured doctrine of *laissez faire* is now dead all over the intelligent world. The modern state not only performs these primary functions, but is also called upon to look after the general well-being of the community—not only in the present but also for the future. It is on account of this changed outlook that the modern state is taking upon itself many activities and functions which once were considered beyond its scope. There is now increasing tendency on the part of the state to interfere in the economic sphere to ensure healthy economic development of the country, and it is also recognized that the state exercises a very profound influence in this direction. People now look more and more to the government to fill the gaps where private initiative does not present itself, and to apply the corrective where some or other evil has crept or is likely to creep in which may be considered to injure the interests of the community. State intervention is now justified in the following cases :

1. Where the business is of monopolistic nature such as railways, posts and telegraph, water, gas and electricity companies. In these cases competition is undesirable, and the state cannot allow double parallel interference with public streets and highways. It is necessary therefore that they should be regulated by government in general interest.

2. Where the private initiative or enterprise cannot be attracted to undertake task because of the remoteness of the reward or unprofitable nature of the enterprise, it is the duty of the state to come forward and to fill in the gap. For example land reclamation, afforestation, building of roads, bridges, and canals are not immediately profitable.

3. Where Control is desirable on account of political consideration, Production of ammunition and armaments for defence cannot be left to private individuals, and this must be taken by the state itself.

4. Where the consumer's interest may be prejudiced or where the individual cannot guard his own interests, the state must intervene to ensure general wellbeing, e.g. in case of drugs, intoxicants, adulteration of foods.

We may now consider the forms which this intervention or relationship of the state to industry may take. The government can influence business in any of the four ways—(1) by giving indirect facilities, (2) by giving direct aid and encouragement, (3) by regulating economic activity and (4) by assuming control and management of enterprise, i.e., nationalisation. Each of them is considered below.

Indirect Facilities. The state renders a signal service to the community by enforcing such laws as relating to contracts, sale of goods, transfer of properties, etc. In their absence business would have been impossible. Economic activity would have been pure gamble where the right would give place to might. The rights, duties and liabilities of the various parties are properly laid down so that smooth running of economic mechanism is ensured.

Another way in which wisely conceived legislation can help trade and industry is to regulate the forms of enterprise. Partnership, companies, societies, holding companies and trusts are all governed by laws. This enables conduct of business in the best and most economical way. Properly enacted legislation relating to the duties and responsibilities of such persons as promoters, directors, managing agents, auditors, trustees and bankers enables a clear understanding of their position, and an element of uncertainty and doubt which would otherwise have been present, is removed, thereby inspiring confidence, and certainty in the public mind. Confidence and certainty are the best driving forces of commerce in the modern world. Further there are the laws relating to bankruptcy and insolvency, settlement of disputes and arbitration, patents, trade marks and copy rights, etc. These all help and facilitate business in one way or other. The rights of the creditors are safeguarded against fraud while the debtor is given protection in difficulty. Laws relating to patents and copy rights afford much needed security and an opportunity to persons to reap the reward of their labours, researches and inventions.

The government provides a sound and suitable system of currency, and weights and measures. Arrangements are made for their inspection and proper maintenance. A well-maintained and stable currency system is extremely essential for healthy growth of business, and smooth working of exchange mechanism.

The state facilitates economic activity by undertaking the collection and compilation of economic statistics, and the publication of reports on industrial and commercial matters, by obtaining information of economic conditions and markets in other countries through its various consular offices, by appointing commissions and committees of enquiry into industrial questions, by organising and regulating local fairs and markets, and exhibitions at home and abroad for furtherance of trade and industry.

The state may undertake research, experiment and investigation. Such bodies may be promoted as Imperial Council of Agricultural Research, Cattle Breeding Centres, Animal Husbandry, institutes experiments in crop diseases, demonstration farms, afforestation and reclamation of land.

State Regulation of Economic Activity. 19th century liberalism involved an attempt to develop an economic policy on the absence of government interference. Enlightened self-interest working under a system of free competition was supposed to bring plenty for all, to benefit the consumer by the lowering of costs, and to secure increasing satisfaction of all human wants which economic goods and services could satisfy. Government control was deemed superfluous. Hopes were, however, falsified. Not only that hopes were not realised, there also sprang up a host of evils, and society was divided into two groups of unequal strength. Poor and weak were exploited by the strong and monopolistic combinations sprang up in place of free competition. It was to meet this situation that government control and regulation became inevitable.

The states today control domestic production, investment at home and abroad, regulate imports and exports, purchasing power of domestic currency and of the foreign exchanges. Factory legislation has become one of the important methods of regulating the industry of protecting the weak against the strong and to ensure the general wellbeing of the masses. By enacting and enforcing such laws as factory acts, Payment of wages act, Trade unions and Trade Disputes Act, Prohibition of employment of children below a certain age, and of women underground or in dangerous undertakings, many of the evils are avoided which would otherwise have crept up. Regulations are laid down regarding hours, minimum wages, and also minimum standards of safety and welfare are fixed. All this is to ensure that production proceeds under healthy conditions, and that health and efficiency of the community is not endangered by requiring women and children to undertake the burden for which they are unfitted. Social insurance legislation is another forward step of modern communities. Workmen's compensation, Maternity benefits, Child welfare, Old age pensions, Unemployment and Sickness insurance are all measures which ensure the wellbeing of those who cannot look after themselves, and therefore it is the duty of the state to provide for them. Liabilities and obligations of employers are laid down in this connection. Laws are made for the safety of the ships, railways, roads and bridges, provision for accidents is made by making it compulsory to insure against third party risks. Limitation of profits and the

rate of dividends, controlling prices rationing of supply, licensing of dangerous industries, ensuring protection against dangerous occupations, making for supply of pure foodstuffs by enacting health laws, are the various measures which are taken by modern governments.

Evolving of a suitable taxation policy is again a pre-requisite of sound industrial development. It should not be regressive, lest it should make distribution of wealth very unequal and concentrate a major portion of community's wealth in the hands of a few individuals, families or classes. It should be on the other hand not so sharply progressive, that it kills initiative to enterprise. The present taxation policy of the government of India kills incentive to economy and efficiency and breeds inefficiency and extravagance.

Direct State Aid Where the private initiative is slow and sluggish, and opportunities for development meagre, the state may come forward, and may provide direct encouragement to private individuals. We find that economic development in other countries is the result of conscious efforts on the part of the state. Japan offers the best illustration of the paternal attitude of the state in fostering industrial development of the country. In Japan there are few modern industries today that do not owe their existence to government initiative. The success of an enterprise lies, as much in the constructive impulse and efforts of the individual, as in the helpfulness and general appraisal of the atmosphere around him, and the conditions in which he has to work. To give only one illustration, it may be found, how the chilling effect of neglect and discouragement from the top can touch an industrial venture at every point of its contact with authority in customs, railways, income-tax, in the administration of factory laws and boiler inspection, in municipal and other cesses, in the purchase of the products for public requirements and public departments, in the arrangement of those numerous details regarding land, sidings, mineral and other concessions, and in a thousand and one ways. A free field and minimum interference by government has involved the concentration of large resources in foreign hands and the consequent creation of a mortgage on the wealth of this country.

Industry may be directly encouraged by government in the following ways —

1. *Protection.* One of the most important means for the development of industries is the protective tariff, i. e., imposing import duties on foreign goods for a definite period. The home industry is thus protected from foreign competition. The indigenous capital and enterprise is attracted to the industry, and industry is developed behind the tariff-wall free from cheap goods of other countries. This practice has now become common, and many countries are resorting to this method to foster the development of their industries.

2. *Subsidies and Bounties.* The state may give subsidies and bounties to an industry in which it is interested either in place of protection or apart from it. Granting of subsidies provides the direct stimulus to the industry.

Bounties and subsidies are sometimes given in place of protection with a view to avoid those risks and disadvantages which protection invariably carries with it.

3. *Exchange Agreements* In order to foster industrial development of the country, the government may use the device of foreign exchanges. The exchanges may be regulated in the interest of the country so that exports will be encouraged, and country in general shall benefit. Further a policy of low exchanges, devaluation or progressive depreciation of currencies may enable a country to give a keen export incentive to its industries. The government of the country can enter into trade agreements, fix quota schemes, and can adopt such devices as reciprocity and preference schemes.

4. *Technical Personnel.* The government may provide facilities for training workers, and also arrangements may be made with other countries to secure technical personnel. This may be placed at the disposal of the industry considered. Technical guidance and advice of experts may be secured from outside through the government.

5. *Financial Aid* This again is important method of help to industrial enterprise. Financial aid may be given in various forms. Government may subscribe to the capital or debentures of the undertaking, may guarantee an interest on the capital, grant a loan, stand as a surety to third parties and make a grant on favourable terms of land, raw materials, firewood or water.

6. *Store Purchase Policy* The government in a country is the largest single customer of any one industry. The various government departments and railways purchase large quantities of all kinds of stores every year and if the government can assure the indigenous enterprise of their sympathetic attitude in this respect, a fairly good demand to the industry is certain. Assurance and certainty of demand for the manufactures of indigenous industry offers keen stimulus to its rapid development.

Nationalization. The final stage of state intervention in business is nationalization where the state takes over the ownership, management and control of an undertaking in its own hands. Almost to all countries all over the world, the public utilities such as railways, water, gas, posts and telegraph, and transport undertakings are already running under the direct control and management of the state. Competition in such undertakings is either undesirable or impossible. In the modern world there has been a swing in favour of collectivism, and it is being increasingly realised that private ownership and capitalist industrialisation are associated with waste and reckless exploitation of the natural resources, and disregard of the public welfare. Demands are being made for the nationalization of key industries including such industries as mining, banking, communications, heavy chemicals and iron and steel, etc.

Objections to State Intervention and Nationalization There have been raised various objections to state intervention in general and nationalization in particular. There are those who point out that the sole cause of our present

ills and economic difficulties is the presence of government interference, while there are others who say that these difficulties are because there is not yet enough of state intervention. The objections against state intervention may be noted below :—

1. The governments, as they are at present constituted in most of the countries, are not qualified to undertake the task. These bodies are primarily chosen for purposes, quite other than that of intervention in industry. Consequently there is little reason to expect in their members any special competence for such a task. "If the government has not the capacity, through regulation to accomplish the easier task of an empire, surely it cannot direct or run the system itself. Men chosen by election for oratorical triumphs and selected by bureaucracy will on an average be no more honest, far less competent, and much more oppressive to liberty than merchants, hawkers and industrialists operating under the law."

2. The present governments are fluctuating bodies whose composition depends upon the results of the next election, and the strength of the various political parties. The various parties coming into power may take steps according to their own whims and party programmes. Their action therefore may be based on short term view, and not extending to the permanent interest of the communities.

3. The areas allocated to public authorities for administration are determined by non-commercial considerations, and therefore they are likely to prove unsuitable for any form of intervention with industry. For example, in India industries and their regulation is entrusted to the Provinces, and if different provinces take different measures within their own areas in regard to a particular industry, the industry will be very differently affected in different areas, and this shall very adversely affect its development. "Administrators are realising that the conduct of business is always an intricate affair, and there is no such thing as one pattern for all industry. Businesses are made in their own molds, and even in the manufacture of brass-headed nails, no two factories turning out these articles are alike in conduct and conditions. In attempting to remedy defects in the minimum wage paid and the length of hours worked in a factory, many other defects might be created which are beyond remedy if the business is to be kept going."

4. Government agencies, in so far as they are elective bodies, are liable to injurious forms of electoral pressure and to personal corruption by private interest. This objection applies both to state intervention through regulation and nationalisation. On the one side, companies, particularly when there is continuing regulation, may employ corruption not only in getting their franchise but also in the execution of it. On the other side, when public authorities themselves work enterprises, the possibilities of corruption are changed only in form, e. g., "every public official is a potential opportunity for some form of self-interest arrayed against the common interest." There are

many instances where vested interests have exerted a good deal of influence, and the policy of the state is moulded to their own advantage at the expense of the rest of the nation.

5. The business of state-owned concerns is managed with a view to winning the applause of the man in the street, and not in a business like manner. The man in the street has a definite voice, and is the master of his masters who cannot dare displease him.

6. State regulation and control prevents the free play of economic forces, and thus creates artificial bottle necks in our otherwise simple mechanism. Those maximum price laws do not help the common people as it is supposed they would. On the contrary, they tend to aggravate the scarcity. Price is like a thermometer, and if you combine it with competition you get something like a thermostat—a more or less automatic regulator of the economic mechanism encouraging production of things for which there is an effective demand, discouraging production of others, serving the comfort and convenience of consumers. But if one is to use it in that way, it is essential to give the regulator a chance. An economist's chief complaint to-day is that the world at large is playing with prices and not allowing their regulator to function.

7. The Superintendent of Insurance, in the Insurance Year Book of 1915, raises certain other objections against nationalisation of insurance and those arguments apply with equal validity to nationalisation of other industries. Nationalisation is suited only to those businesses where the work is of routine nature, and the goods or services supplied are of every individual's need. In other cases where new grounds have to be broken, governments have proved unequal to the task. "The highly advanced stage of development reached and the high standard attained by the business of insurance in all its forms are due to private enterprise. An officially run insurance department is apt to remain satisfied with a static state of affairs and not being subject to the stress of competition, would merely keep itself to the trodden path. From its very composition it would be incapable of taking quick decisions and acting on them, a course so very essential for progress. For even if the officer at the head considered the adoption of a particular course desirable, others unconnected with that department would have a large say as every problem connected with one department is likely to have a bearing on the work of some other department.

8. Another serious disadvantage of government would be that the very great personal interest characteristic of private enterprise and the unceasing attention paid to efficiency of administration so that maximum results might be obtained at the minimum outlay, would be absent. Combination of business units into one large unit would eliminate competition, would conceal inefficiency, and would deprive the administration of the advantage of healthy comparisons with rivals to see in what direction it could improve its efficiency to bring down overhead costs.

Arguments for Nationalisation

1. The personal interest of the head of the business, and its incentive to efficiency is only present in small business. Over a large field of industry, however, there is choice between joint stock companies and public concerns. Personal interest is present in neither of the two. "There are no particular reasons why the financial results from private or public operation should be different if the conditions are the same." There seems no general ground for holding without reference to the special nature of an undertaking, that either public or private management is likely to prove technically the more efficient. On the other hand to some extent public authority has the advantage. Good technical and expert services can be obtained at smaller cost because of the attractiveness of public service.

2. Public operation of industries does not necessarily imply that the industry is run by a government department organised on civil service principles. An organisation like the post-office directorate may run the show and it can compare very favourably with the directorate of joint stock companies.

The arguments of the opponents lose much of their force when it is remembered that government undertakings may be run by bodies of men appointed for the express purpose of industrial operation or control. These persons may be chosen with reference to their fitness for the task, their appointments can be for long periods, the area allotted to them can be suitably adjusted, and their terms of appointment can be such as to free them, in the main, from electoral pressure.

3. The case for nationalisation is specially strong where the industry or undertaking in question is concerned with public health and well-being, where quality is essential and inspection difficult. Further where the typical unit is large tending towards monopoly, and where the industry has been reduced more or less to routine and in which there is comparatively little scope for daring adventure.

4. Nationalization offers an additional source of revenue to the state.

5. Lastly private individual and his acting self-interest cannot be trusted to ensure the general well-being of the community and for this it is essentially desirable that state must exercise some sort of control in order to see that private enterprise does not indulge in restricting production for purely selfish gains, ignoring the interests of the consumers and the country. A *laissez faire* policy, glorified by economic theory as the solvent of all ills and foundation of all prosperity, has distressingly failed to achieve what it claimed. The industrialism of last 40 years, with its restriction of production, its wanton destruction of commodities, its paradox of poverty in the midst of plenty, has made the continuance of *laissez faire* policy impossible. Industrialism has now reached a stage when systematic planning and centralised control are necessary both for the purposes of production and equitable distribution.

State and Industry in India

A brief review of state policy towards industry in India may here be made. In the beginning of British rule in India the East India Company's Commercial instincts made it, at first, favour those Indian industries on which its export trade depended. But owing to the pressure of vested interests in the home country, this policy was given up and India began to be looked on as a source of raw materials for the manufacturing industries of England.

The East India Company ceased to exist and the government of the country was transferred to the Crown but the policy of the Company continued unchanged. *Laissez faire* was the order of the day in England and the same traditions were brought to bear in our country. To regulate industry was pernicious, to assist it was futile and to participate in it was waste of public money. Thus the one salient characteristic of our economic life during the past 100 years has been a persistent adherence on the part of the government to the traditional policy of *laissez faire*. Sometimes the state did show interest in the industrial development of the country but it was fitful and haphazard, and the authorities at home always insisted that government should remain aloof from such activities.

It was in 1905 that a separate Imperial Department of Commerce and Industries was created at the instance of Lord Curzon. Some provincial governments like the U.P. and Madras, also began to take interest. After the Industrial Conference of 1909 at Ootacamund, the Madras Government appointed a Director of Industries. These attempts were however, readily discountenanced and seriously deprecated by Lord Morley, the then secretary of state. He pointed out that the state should confine itself to industrial instruction and should avoid all semblance of commercial venture. Lord Cromer, the successor of Lord Morley, was a bolder person and he allowed the government to maintain experimental plant but the Government of India could not do much in this direction. The Swadeshi movement which was at its height in this period, failed, lack of government support being one of the most important causes.

The outbreak of war of 1914-18 brought about a change in this policy. European markets for raw materials were closed down, and the danger of dependence on foreign supplies was realised. The military importance of developing the economic resources of the country was brought to light by the war and the theory of *laissez faire* was discarded once for all, and its place was taken by direct state encouragement. The Indian Industrial Commission was appointed in 1916 to examine the possibilities of industrial development in India. The Commission emphasised the supreme importance of state aid to industries, laying special stress on chemical, electrical and machine-tool industry. In February, 1917 Government of India created the Indian Munitions Board to control and develop Indian resources with special reference to the needs created by the war. Not much was done upon the recommendations of these bodies. The few industries, that were started during the war period, decayed afterwards owing to

the fierce competition of other advanced countries.

After the constitutional reforms of 1919, industries became a provincial subject, and provincial governments began to put forward positive efforts to help industrial development. The various measures adopted by Provincial governments and the Central government taken during the inter-war period may be seen below :—

State Aid to Industries. The Government of Madras passed State-aid to Industries Act in 1922, which was meant to provide financial and other help to cottage and other industries. In 1923, a similar measure was adopted in Bihar, which also provide for the supply of machinery on hire-purchase basis. Subsequently such acts have been passed in Bengal in 1931, C.P. 1934, Punjab and U.P. 1935. As regards the working of these acts, the aid has been given to numerous and varied enterprises, but the achievements have not been very spectacular. The cottage and small industries found it extremely difficult to avail themselves of the facilities. In Bihar no enterprise aided between 1924-28 except one was surviving in the hands of original owners. Most of the aided industries could not make any profit, and were unable to meet their debts according to the terms of the Act. The scheme of advancing machinery under hire-purchase system has also proved disappointing and the Industries Department has become a "museum of obsolete machineries."

Industrial Education. Although the Victoria Jubilee Technical Institute, Bombay was set up in 1877, the subject of technical and vocational education has been largely neglected in our country. It is only recently that the importance of sound technical education has been realised, and efforts are being made to remedy the defect. In 1901, at the instance of Lord Curzon, a number of technical scholarships were instituted. Since the subject has received from time to time detailed attention of various commissions and committees, viz., Industrial Commission 1916-18, the Calcutta University (Sadler) Commission, Committee appointed by government of Bombay 1921 and 1935, the Zakir Hussain Committee 1937 and of M/s. Abbot and Wood, educational experts from England, 1937. Indian School of Mining at Dhanbad was opened in 1926 for training of mining engineers and geologists. Bombay University has opened an institute of textile technology. Other technical institutes have also been established, such as Hosiery Institute at Ludhiana, Silk Institute at Bhagalpur, and Cottage Industries Institute at Gulzaribagh. During the war a scheme of technical training, known as Bevin's Technical Training Scheme, was taken up in which batches of workers were sent to U. K for technical training in British factories. The present position in regard to general commercial and technical education, however, remains very unsatisfactory, and the actual provision that has been made by government or private effort can scarcely be called adequate considering the size and requirements of the country.

Protection. Indian opinion has been always favouring a policy of protection for the development of indigenous enterprise. The question of

protection was examined here in 1921 by a fiscal commission. The Commission recommended a policy of discriminate protection to be administered through a body called the Tariff Board. The recommendation was accepted by Government of India in 1923. A Tariff Board was set up to examine the claims of various industries for protection, and on the recommendations of the Tariff Board, protection has been afforded to a number of industries, such as iron and steel, sugar, paper and cotton. This has helped those industries to develop and saved some from destruction. The measure, however, has been a halting one and not met with the full approval of Indian public. Even this half-hearted measure has not been applied consistently, and protection has been refused to several industries on various grounds. The inclusion of India in the orbit of Imperial Preference has brought about the anomalous position of "protection within Preference" which has neutralised to some extent the benefits of protection. "The influence of Manchester Capitalists is written large in Indian Tariff history. They have been as anxious to preserve the Indian market for the benefit of British manufacturers, merchants, bankers and shippers, as American Capitalists have been to preserve the American market for themselves." (Buchanan: Development of Capitalist Enterprise in British India).

Industrial Research. Industrial Research Bureau was set up in 1935 with a research branch at Alipore. The Bureau is attached to the Indian Stores Department, and can avail of the advice of Indian Research Council. Its functions are the collection and dissemination of industrial intelligence, collaboration with industry in industrial research, the publication of appropriate bulletins giving advice with a view to industrial standardization, and assistance in the organization of industrial exhibitions. During the war Board of Scientific and Industrial Research has been set up to promote research.

Stores Purchase Policy. The various government departments and railways purchase huge quantities of all kinds of stores every year, and till recently these purchases were made abroad. On the recommendation of Industrial Commission a Stores Purchase Committee was appointed. Steps are now taken to see that goods are purchased in India and Indian industries encouraged. Local purchasing agencies have now been created at Calcutta and Bombay, and inspecting agencies at Madras, Bombay, Karachi, Cawnpore and Delhi.

It is clear from the above that though the state now is taking definite steps to develop Indian industries, progress has been not quite satisfactory. No comprehensive view of the whole industrial sphere is yet taken. The state must create conditions congenial enough for the industries to thrive so that the economic resources of the country are best made use of.

The outbreak of second world war in 1939 created a far more urgent demand for industrial production than had the war of 1914-18. It became urgently necessary to develop India into arsenal for allies if war in the East

was to be successfully terminated, and if supplies were to be regularly maintained. The Eastern Group Conference, the Report of the Grady Mission and the appointment of a number of technical committees may be regarded as war measures, the main object of which has been the co-ordination of war effort. But the Government did not take any special step to put these war-time developments on a permanent footing.

Government of India's Post-war Industrial Policy. After the termination of hostilities, post-war planning was much in the air, but the Government of India took complacent attitude of the whole matter. It was on account of the insistent public demand that Government of India created the Planning and Development Department. The department set up various reconstruction committees and prepared schemes for post-war reconstruction. In April 1945, the Government of India came out with a statement of their industrial policy which, at the very out-set, stated that the fundamental objects of industrialisation were threefold, namely, (a) to increase the national wealth by maximum utilisation and exploitation of the country's resources. (b) to make the country better prepared for the defence and (c) to provide a high and stable level of employment.

In order to achieve the above objects, the Government decided to abandon *laissez faire* policy, to develop some basic and heavy industries, to formulate a tariff policy appropriate to the post-war needs and conditions of the country and to nationalise basic industries of national importance, apart from ordinance factories, public utilities and railways.

The Government of India also decided to assist industry in one or more of the following ways:—

- (1) By making loans or by subscribing a share of the capital in industrial undertakings which are considered to be of importance to the country's development, but for which adequate private capital may not be forthcoming.
- (2) By guaranteeing a minimum dividend on capital or undertaking to meet revenue losses, for a fixed number of years, subject to the condition that Government would have a voice in the management and that a ceiling will be fixed for the return on capital.
- (3) By giving adequate financial support to research organisations set up by industrial associations representing organised industries.
- (4) By buying Indian industry's products in preference to others subject to reasonable safeguards as to quality and price.
- (5) By promoting an Industrial Investment Corporation or a similar institution.
- (6) By examining from time to time, the tax system with a view to ensuring that, while securing the ends of social justice and national budgetary interests, the taxation does not act adversely on the development.
- (7) By assisting in the procurement of capital goods required by industrialists from foreign countries,

(b) By making the services of exports available to industry,

Government also decided to take power to license industrial undertakings in order to regulate the growth of industry. It is a well-known fact that one of the serious defects of this unregulated freedom to promote industrial enterprise has been the concentration of industries in certain areas. The effects of such concentration have been of far-reaching economic, social and strategic importance. The Government also proposed to undertake, apart from licensing, other controls to achieve the following objects:—

(a) To secure balanced investment of available capital resources in industry, agriculture and the social services.

(b) To secure for industrial workers a fair wage, decent conditions of work and living and a reasonable security of tenure.

(c) To prevent excessive profits to private capital

(d) To ensure the quality of industrial products by enforcing standardisation of products in the interest of both internal and external markets.

(e) To ensure that unhealthy concentration of assets in the hands of a few persons or of a special community would be avoided.

(f) To require necessary technical training of personnel and to extend the benefits of such training to minorities and backward communities.

Though this statement did not clarify many important issues, yet it constituted an important milestone in the advance of the country towards industrialisation. For the first time, the Government of India decided to abandon *laissez faire* policy and take direct interest in the industrial development of the country.

Government of India's new Industrial Policy.

The Industrial Policy of Government of India was enunciated on the 6th April, 1948, and it avoids the two extremes of reactionary conservatism and revolutionary socialism. The statement of policy sets out the broad objectives of Government's policy in the industrial field, demarcates the respective sphere of State and private enterprise, clarifies Government's policy in regard to the role of labour and foreign capital and indicates the steps Government propose to take for carrying out their policy.

The resolution states that the Government of India have given careful thought to the economic problems facing the country. The nation has now set itself to establish a social order where justice and equality of opportunity shall be secured to all people. The immediate objective is to provide educational facilities and healthy services on a much wider scale, and to promote a rapid rise in the standard of living of the people by exploiting the latent resources of the country, increasing production and offering opportunities to all for employment in the service of the community.

While stressing the need for securing an equitable distribution of wealth, having regard to the present state of the nation's economy, Government's policy will be first to step up production, particularly of capital equipment, of essential

consumer goods and of commodities the export of which will increase foreign exchange resources.

The resolution goes on to classify industries into four broad groups. The first one concerns the manufacture of arms and ammunition, production and control of atomic energy and the ownership and management of railway transport. These are to be the exclusive monopolies of the Government. The second group deals with coal, iron and steel, aircraft manufacture, ship-building, mineral oils, manufacture of telephone, telegraph and wireless apparatus excluding radio receiving sets. Here the State (which in this context includes Central, Provincial and State Governments and local bodies) will be exclusively responsible for the establishment of new undertakings, while private enterprise will be left free to develop the existing units for a period of ten years. But if at the end of this period Government will decide to acquire any of these units, due compensation will be paid on a fair and equitable basis. The third group treats of 18 major industries, which, though subjected to regulation and control of the Central Government in consultation with the Provincial and State Governments concerned, would be in the hands of private enterprise. The rest of the industrial field, which constitutes the fourth group, will normally be open to private enterprise, individual as well as co-operative. The State will progressively participate in this field, nor it will hesitate to intervene whenever the progress of an industry under private enterprise is unsatisfactory.

Next The Central Government will also promote enterprise like large river valley developments, which are multi-purpose projects of great magnitude, involving extensive generation of hydro-electric and irrigation on a vast scale and are calculated in a comparatively short time to change the entire face of large areas in the country. Projects like the Damodar Valley Scheme, the Kosi Reservoir and the Hirakud Damitram will come under this class. The Government will also undertake the production of fertilisers on a very large scale and have in view other enterprises like the manufacture of essential drugs and of synthetic oil from coal.

The Government recognise the very important role to be played by cottage and small scale industries in the national economy, offering as they do scope for individual, village or co-operative enterprise, and means for the rehabilitation of displaced persons. These industries are particularly suited for the better utilisation of local resources and for the achievement of local self-sufficiency in certain types of essential consumer goods. The healthy expansion of cottage and small-scale industries depends upon a number of factors, like the provision of raw materials, cheap power, technical advice, organised marketing of their produce, and where necessary, safeguards against intensive competition by large scale manufacture, as well as on the education of the worker in the use of the best available technique. An important objective will be to give, as in China, a distinctly co-operative bias to this field.

In matters arising from the problem of labour *versus* capital Government

have accepted the resolution on the subject, passed by the Industries Conference, which states *inter alia* that "the system of remuneration to capital as well as labour must be so devised that while in the interest of the consumers and the primary producers, excessive profits should be prevented by suitable methods of taxation and otherwise, both will share the product of their common effort, after making provision for payment of fair wages to labour, a fair return on capital employed in the industry and reasonable reserves for the maintenance and expansion of the undertaking." Government also consider that labour's share of the profit should be on a sliding scale normally varying with production, and further propose to establish machinery which will function at different levels, viz., Central, regional and unitary for advising on fair wages, fair remuneration for capital and conditions of labour. Government also intend to take steps to associate labour in all matters concerning industrial production through the creation, for each major establishment, of production committees and works committees consisting of representatives of worker and employers in equal numbers.

As regards foreign capital and foreign enterprises, Government recognise the value of the need for both, particularly of the latter, and will be initiating suitable legislation regarding the conditions under which they may participate in Indian industry, one of the important conditions will be that, as a rule, the major interest in ownership and effective control should always be in Indian hands and that, in all cases, the undertakings concerned will train suitable Indian personnel for the purpose of eventual replacement of foreign experts.

With a view to increasing production and speeding up industrialisation, Government have decided to remove transport difficulties, to facilitate the import of essential raw materials to the maximum possible extent, to design the tariff policy so as to prevent unfair competition and to promote the utilisation of India's resources without imposing unjustifiable burdens on the consumer, and to review system of taxation and to readjust it where necessary with a view to encouraging saving and productive investment and preventing undue concentration of wealth in a small section of population. Government also propose to establish a National Planning Commission whose main function will be to formulate and execute programme of development, calculated to achieve the ultimate aim of promoting a rapid rise in the standard of living of the people.

This statement of Industrial policy was well-received by the industrial circles because it removed two of their most outstanding fears in declaring that no immediate nationalisation of industries would be made and remaining silent about the demand for the abolition of Managing Agency system. But still the principle objective of this great concession has remained unfulfilled; increase in production has not taken place. The industrialists, on the contrary, have taken the liberalism of the Government as its weakness and have succeeded in frustrating the Government's main purpose in the resolution.

Test Questions

1. What do you wish to be the relation of State to industry in free India?
Discuss thoroughly. (Agra B. Com. 1948)
2. Discuss the various ways in which the government may help Indian industries in the post-war period. (Agra B. Com. 1946)
3. What in your opinion should be the attitude of the State in relation to industry? Illustrate your answer with reference to conditions in India. (Rajputana B. Com. 1949)